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THE
ACCOUNTANT'S DICTIONARY

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THE ACCOUNTANT'S DICTIONARY

A COMPREHENSIVE ENCYCLOPAEDIA AND
DIRECTION ON ALL MATTERS CONNECTED
WITH THE WORK OF AN ACCOUNTANT

ILLUSTRATED WITH THE NECESSARY FORMS AND DOCUMENTS

Edited by FRANCIS W. PIXLEY, F.C.A.

Of the Middle Temple, Barrister-at-Law

AUTHOR OF

"AUDITORS: THEIR DUTIES AND RESPONSIBILITIES"; "ACCOUNTANCY";
ETC., ETC.

WITH CONTRIBUTIONS BY EMINENT AUTHORITIES
ON ACCOUNTANCY AND ACCOUNTANCY MATTERS



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THE ACCOUNTANT'S DICTIONARY

FOR]

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FOREIGN BRANCH ACCOUNTS.

(See BRANCH ACCOUNTS.)

FOREIGN CREDITORS.

(See BANKRUPTCY ACCOUNTS, p. 159.)

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FORM OF ACCOUNTS.

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FORWARD BARGAINS.

(See FINANCIAL HOUSES AND INVESTORS, ACCOUNTS FOR, p. 484.)

FRAUD.

Used in its commonest sense, this word is generally taken to denote some dishonest dealing, and, as such, it has an exceedingly wide signification ; indeed, any departure from strict honesty is often described as fraud. In its legal sense, however, the meaning is somewhat more restricted, and fraud has come to mean, generally speaking, a false representation of facts, made with a full knowledge of its falsehood, or made recklessly without any belief in its truth, or not caring whether it is true or not, with the intention that such representation should be acted upon by the party who is defrauded, and actually inducing him to act upon it. This appears to sum up the

effect of the judgment in the case of *Derry v. Peek*, 1889, 14 App. Cas. 337, and sums up the position of ordinary individuals. But since the case just named, it has been felt essential to make the question of fraud a more stringent matter when the directors of a joint stock company are concerned. First, by the Directors Liability Act, 1890, and afterwards by the Companies (Consolidation) Act, 1908, which repealed and re-enacted (*inter alia*) the provisions of the Act of 1890, if a charge of fraud is now made against directors, it is not for the plaintiff in an action, who is the person defrauded, to prove that the directors of the company had no grounds for believing in the truth of the statements contained in a prospectus, which are alleged to be fraudulent, but for the directors to show that they had good grounds for making the statements.

It must be remembered that in order to avoid a contract on the ground of fraud, the fraudulent statement complained of must be one of fact and not of law, must have been made by one of the parties to the contract, and must have been the cause of the contract being entered into. The misrepresentation must have actually deceived the party injured, and some damage must have been suffered.

Fraud is a good ground for seeking to avoid any contract or to set aside a deed, or, in fact, to render void any transactions which have been entered into by reason of the same. In cases of agency, a principal is always responsible for the fraud of his agent if such fraud was connected with the business of the agency. One special point must be carefully borne in mind. Whenever a question of fraud arises, the person defrauded must act with the utmost diligence, otherwise he may be considered to have waived his rights. Again, the person who alleges fraud must come with clean hands. He cannot expect to be heard successfully if his own conduct is not thoroughly satisfactory. (See also FRAUD AND FALSIFICATION OF ACCOUNTS.)

FRAUD AND FALSIFICATION OF ACCOUNTS.

INTRODUCTION.—This subject is one of intense interest from whatsoever point it is viewed. Through the pages of history one finds in almost every chapter that there have been persons capable and willing to perpetrate frauds. Perhaps one of the earliest instances of deceit or imposture—for this is the meaning assigned to the word “fraud” in the ordinary dictionary—is that of Jacob, who by means which are familiar to all, deliberately deprived his brother Esau of his birthright, with the intention of reaping the benefits which were not his by right. And this is really the motive underlying the majority of frauds, namely, to obtain some advantage which could not be gained by means other than dishonourable. The above incident was one of comparative simplicity in execution, but in the course of time, as nations developed and society became more complex, fraud has also developed and assumed other phases. The simple fraud and plain embezzlement, whilst continuing to a great extent, have also been combined with misstatement and falsification of accounts. It is this modern development of fraud which it is proposed to deal with in the present article.

To the professional man engaged in the investigation of the fraud, whether he be counsel, solicitor, or accountant, the preparation of the case against, and possibly the prosecution of the defaulting party, the matter is not only full of interest, but frequently taxes his skill to the utmost, whilst underlying all is the human element—the pathos and the tragedy—in the case. It is in this direction that possibly the accountant has an advantage over his professional friends of the two branches of the legal profession, in that, unless the delinquent has temporarily disappeared, or has passed beyond the bounds of punishment by his fellow men, the accountant must come into closer personal contact with him, and probably also at an earlier stage, than either the solicitor or counsel. In such cases it is the accountant who ascertains where and when the first step was taken which has led to the degradation and social ruin of the delinquent; it is he who ascertains what was the first temptation which led to the falling away from the paths of rectitude, and hears of the vain attempts made to cover up and possibly correct the earlier lapses; to him are probably confided the hopes and ambitions which buoyed up and spurred on the unfortunate defaulter in his earlier days, before the temptation or opportunity came to attain his ends by easier but less honourable means, which have led to such disastrous results, and to him is poured out the poignant sorrow and vain regrets of the broken home and the blank

and dismal future—all realised, unfortunately, when it is too late to make amends—when the one flaw in the possibly otherwise skillfully conceived fabric of fraud has been discovered. It is on this account that the work of the accountant in connection with investigations to discover or unravel fraud is of such deep interest, often tempered with sadness at the causes which led to its inception, and in most cases also tempered with sympathy with the delinquent and those whom he may have also ruined—financially and socially—in his own fall.

DEFINITION OF FRAUD.—The Courts of Equity, considering that the ways of fraud are infinite, and new modes of committing it are constantly arising, have refused to give a definition of the word. Lawyers, however, have not been so reticent, and various definitions of fraud have been given from time to time, the most comprehensive and generally accepted being probably that of the late Sir William Anson—

“Fraud is a false representation of fact made with a knowledge of its falsehood or recklessly without belief in its truth, with the intention that it should be acted upon by the complaining party and actually inducing him to act upon it.”

On the other hand, the Falsification of Accounts Act, 1875 (38 & 39 Vict. c. 24) provides that—

“If any clerk, officer, or servant, or any person employed or acting in the capacity of a clerk, officer or servant, shall wilfully and with intent to defraud, destroy, alter, mutilate or falsify any book, paper, writing, valuable security, or account which belong to or is in the possession of his employer, or has been received by him for or on behalf of his employer, or shall wilfully and with intent to defraud, make, or concur in making, any false entry in, or omit or alter or concur in omitting or altering, any material particular, from or in any such book, or any document or account, then in every such case, the person so offending shall be guilty of misdemeanour, and be liable to be kept in penal servitude for a term not exceeding seven years, or to be imprisoned with or without hard labour for any term not exceeding two years.”

Special provision for the punishment for falsification of the accounts of certain classes of undertakings has been provided for under the “Building Societies Act, 1894,” “Industrial and Provident Societies Act, 1893,” “Friendly Societies Act, 1896,” and “Collecting Societies and Industrial Assurance Companies Act, 1896.”

Fraud and falsification may be committed by intentional errors of omission, commission or principle, all of which will be dealt with in regard to their bearing on accounts. Frauds of a certain nature may also be committed in connection

with the statistical books of companies, but it is not proposed to touch upon this branch of fraud in the present article. Furthermore, falsification of books may be carried out either with the object of concealing the true trading results of a business, or with the intention of covering up an actual embezzlement of cash or money's worth.

DEFINITION OF EMBEZZLEMENT.—The definition of "Embezzlement" (24 & 25 Vict. c. 96, s. 68) is—

"Whosoever, being a clerk or servant (or being employed for the purpose, or in the capacity, of a clerk or servant) shall fraudulently embezzle any chattel, money, or valuable security, which shall be . . . taken into possession by him for, or in the name, or on the account of, his master or employer . . . shall be deemed to have feloniously stolen the same from his master or employer; although such chattel, money, or security, was not received into the possession of such master or employer otherwise than by the actual possession of his clerk, servant, or other person so employed."

It is interesting to notice two distinctions that are drawn in law on the question of what is commonly termed "embezzlement" of cash or money's worth "at the point where "possession" becomes a factor in the case. A servant can only "embezzle" that which he has received *for* his master, whereas if he takes to his own use that which he has received *from* his master, he commits a "larceny." Consequently, if a cashier misappropriates money that he has received from a customer, even though he obtains it through a third party—a traveller or collector—he is guilty of embezzlement, since the money has not been received into the *actual* possession of his master, but in this case if the cash had been placed in the till before it was taken, the crime becomes one of larceny. On the other hand, if his master hands him a cheque to cash and use for certain purposes, such as the payment of wages, and he then misappropriates the whole or part of the money to his own use, he commits a larceny, for he has taken it from the possession of his master. Before more modern legislation rendered it less necessary to determine for which offence a man should be indicted, this point of "possession" became so involved that justice frequently failed owing to some small legal technicality being raised which had the effect of showing that the indictment was based on erroneous grounds.

Since "embezzlement" and "larceny" in connection with such frauds as are most common in the practical experience of professional accountants, are separated to a great extent only by a very slight legal point, it is well to here give a definition of what the latter term has come to

mean from the point of view of the legal mind. This definition will help to emphasise the distinction mentioned above when compared with that of "embezzlement"—

"When any person takes, and carries away—or when a bailee appropriates—another person's personal chattel, of some value, without any claim of right, and with an intention to deprive that other person of the whole benefit of his title to the chattel."

MODES OF FRAUD.—Perhaps the most serious class of fraud is that carried out by those responsible for the management of a company, when they are parties to the issuing of false and misleading Balance Sheets. Until the Companies (Consolidation) Act, 1908, became law it was not necessary that the Balance Sheet issued by a limited liability company should be signed by any of the directors, although it was frequently done in practice. Clause 113 (Subsection 3) of the Companies (Consolidation) Act, 1908, provides that every Balance Sheet issued by a limited liability company shall be signed on behalf of the Board by two directors of the company, or, if there be only one director, by that director. Formerly, accounts which had been prepared by a managing director were very frequently issued without being considered by the other directors at all, or were passed hurriedly by them at a Board meeting, without any investigation being made into the details of the Balance Sheet, with the result that, with the exception of the one director who was responsible for its preparation, very few of the directors knew anything of its contents. Sometimes, on subsequent investigation, it was discovered that the figures inserted against certain items in the Balance Sheet were, if not fictitious, at least grossly inflated, with the result that in many cases heavy loss was suffered by the creditors and shareholders of the company. When this has happened, it has generally occurred where a group of companies has been under the guiding hand of one individual who has acted as managing director, and sometimes as chairman also, the other directors being merely puppets in his hands. A noteworthy example of fraud of this nature was the manipulation of the accounts of the London and Globe Finance Corporation and its allies, the Standard Exploration Company and the British American Corporation, which resulted in a total loss of the whole of the shareholders' capital amounting to several million pounds, and the loss also of practically the whole of the creditors' money, a far more serious matter, because shareholders in companies of this nature know that they are running very considerable risks in order to obtain a large return, even in cases where companies are well and honourably managed.

It is not within the scope of this article to enter

fully into the details of individual cases, but as regards this particular fraud, there are one or two points that may with advantage be recalled. This was, perhaps, one of the most gigantic frauds that has ever been perpetrated upon the public. The trial, which, with its tragic sequel, will be well remembered by most readers, disclosed manipulations that would scarcely be credited. The 1899 Balance Sheet showed "Cash at Bankers" amounting to £534,000. Of this sum something like £360,000 was provided by one of the allied companies within three days of making up the accounts, mostly on account of so-called purchases of shares. Before a month had elapsed, the balance was reduced to £56,000. The position at 30th September, 1900, the end of the financial year, was such that it would have been inconvenient to close the books at that date, for there would have been shown a loss of over one and a half millions sterling. Accordingly transactions were again entered into with other companies and a Balance Sheet was made up as at 8th December, showing amongst many other manipulated items, "Shares in other Companies, £2,332,632 0s. 1d." The assets were inflated to such an extent that the true loss was converted into a "profit" of nearly half a million. From this Balance Sheet also liabilities on the Stock Exchange amounting to considerably over £1,500,000 were omitted by the "simple" process of passing invalid resolutions.

It will therefore be seen that the assets were fraudulently overstated for the purpose of deliberately making the accounts appear more favourable than they otherwise would have done, with the object of paying dividends and thus maintaining the market value of the shares of the company and carrying it over an awkward period of its career, whilst incidentally securing to the directors for a further term the payment of their remuneration.

However, the perpetration and subsequent discovery of the London and Globe Finance Corporation and similar frauds, in spite of the terrible results that accrued to those who were deceived, proved to be ultimately a benefit to society, for the legislature was awakened to the fact that a considerable strengthening of the law in this respect was urgently necessary to protect, not only the investing public, but those who trade with limited liability companies.

LIABILITY OF DIRECTORS, PROMOTERS, ETC.—Those in control of bodies corporate or public companies, since the passing of the Larceny Act, 1861, have been subject to punishment for fraudulently appropriating property; keeping fraudulent accounts, wilfully destroying books, etc., or publishing fraudulent statements; but the later Companies Acts, now codified in those of 1908 to 1917, render any misdeeds by those in command a much more dangerous undertaking. In

fact, in one respect, a prosecution for fraudulent representation under the Companies Acts is an easier matter to prove than is the case in dealing with a private individual. In the latter case it is necessary to establish that the defendant was fraudulent, whereas by the Companies (Consolidation) Act, 1908, s. 84, directors, promoters, and persons who have authorised the issue of any prospectus or notice with regard to a company are liable to loss or damage caused by an untrue statement therein to any person who has subscribed for any shares or debentures on the faith of such prospectus or notice, unless it is proved (a) that they not only believed in the statement, but had reasonable grounds for such belief; or (b) that it was a correct statement of the report or valuation of an engineer, valuer, accountant, or other expert; and even then they will be liable if it be proved that they had no reasonable ground for believing that such person was competent to make such a report or valuation; or (c) that such a statement was a correct and fair representation of a statement made by an official person or contained in a public official document.

It will be seen that the effect of this clause is practically to make carelessness on the part of directors and promoters, ground for an action for fraudulent representation.

There are further sections of these Acts which give protection against directors and promoters which may be briefly summarised—

Sec. 175 where power is given in England to order the public examination of directors, promoters, etc., as to the formation or conduct of the business of the company.

Sec. 215, giving power to the Court to assess damages against delinquent directors, etc.

Sec. 216 providing for punishment for falsification of books, etc.

Sec. 217 giving power for prosecution of delinquent directors, etc.

Each of the above sections refer to companies in the course of liquidation.

Sec. 281, where a penalty is imposable upon those liable for any false return, report, certificate, balance sheet, or other document.

Again, frauds are sometimes committed by high officials of companies under circumstances which do not result in the gain of any enormous sum of money to the delinquent, and which possibly only indirectly affect him, when, for instance, a manager or managing director, not being paid a commission on the results of his management, may falsify the accounts of the undertaking merely with the view of showing good results and thus retaining his position, or in any event, avoiding unpleasant criticism. Such was the position in the Millwall Docks case, where, except in the earlier years of the fraud, when the

manager received a small commission on profits, the sole advantage derived by the responsible party was that he retained his position as managing director. In this case the falsification took the form of over-estimating the assets (*i.e.* book debts); equally reprehensible, however, would have been the inflation of the stocks on hand or the under-estimation of the liabilities by the suppression of invoices for goods ordered and delivered.

Under this heading it might be convenient to add a few remarks on certain matters of account which could not be said to be frauds in the strict sense of the word, but which, viewed in the light of the ultimate effect that such actions have upon the financial stability of the particular undertaking, and the object for which they are doubtless so treated, are, to say the least, something in the nature of misrepresentation.

INFLATION OF ASSETS.—It frequently happens that it becomes necessary to replace assets in the nature of buildings, plant, etc. It is well recognised that only such proportion of the expenditure as represents the added value of the asset should be capitalised. In other words, the original asset, less the value of any old materials sold or utilised in the new construction, should be written off against revenue, and the actual costs of the new asset placed to capital. Now the Board, to enable them to show substantial profits in the past, may have neglected to make adequate provision for the wastage in the value of the original asset, and they are accordingly faced with the proposition as to whether they will disclose the true state of affairs by writing off the amount standing in the books on the old account, or capitalise the whole of the expenditure without dealing with the cost of the original asset, which has ceased to exist. It is easily seen how the opportunity may be taken to misrepresent the true situation.

There is another point of a similar nature, *i.e.* the charging to capital expenditure of amounts which are rightly of a revenue character. It is frequently found renewals are deliberately capitalised on the ground that the value of the property is thereby increased, but really because if such payments were properly treated, the results of trading would be so unsatisfactory that confidence in the management would probably cease to exist.

Carrying forward a proportion of expenditure is also a favourable method of concealing bad trading. This frequently arises in the case of current advertising. The initial cost of placing a new product on the market may quite rightly be spread over a short period of years, but immediately the article has become established, further expenditure is properly chargeable against the period in which it is made. Any other method is delusive.

From the foregoing, it must not be inferred that all frauds committed by those in charge of the control or direction of a company must of necessity be carried out by the inflation of the assets of the business, or the understatement of its liabilities. Cases occur where, for reasons well known to, and carefully considered by, themselves, it is possible for those in control of a company to understate intentionally the profits, and less frequently to overstate the liabilities, with a view to depressing the price of the shares, so that they may be thrown on the market by weak holders and sold for considerably less than their real value, as the outside shareholder would not have the same opportunities as the directors of ascertaining the intrinsic merits of the undertaking. In this case, were the Transfer Register examined, it would be seen that the shares when sold were probably purchased by those in control of the company.

Similarly, the profits of successful undertakings are frequently understated even with the knowledge of the whole of the shareholders, under the guise of "strengthening the financial stability of the company." As to how far such strengthening should be insisted upon by a controlling majority of shareholders represented on the directorate, in the face of opposition on the part of the minority of shareholders, is a very moot point, especially in cases where it can be traced that all shares coming on the market have passed the hands of the controlling majority.

Further, there is a well recognised practice of depreciating to such an extent that valuable assets are written down to a nominal figure, and so creating "secret reserves." Whilst the advisability of such a proceeding is generally admitted in the case of banks and similar institutions, it is a debatable point as to whether such financial prudence does not carry with it an element of danger in the case of undertakings of less repute than those referred to in view of the fact that it *may* pave the way to irregularities by those in control, which might operate hardly on succeeding shareholders.

INFLATION OF ACCOUNTS.—A source of fraud which does not involve embezzlement and possibly also not the actual falsification of accounts, is the inflation of accounts by vendors who are disposing of their business, either to another firm or to a limited liability company formed to take over the same. Some of the means of increasing the profits in such circumstances are by the vendors paying business expenses out of their own private pockets, charging consignments to their agents at selling prices, and thus securing the profit on the goods when they are subject to return in the event of their not being disposed of; large returns, after the close of the financial year, of sales made prior to the close of the year and being returned into stock after the

close of the year, not allowed for when closing the accounts, whereby the gross profit on such goods is erroneously taken credit for, and the inclusion in the sales of absolutely bogus sales for which no payment is likely to be made.

Several examples of the first-mentioned class of fraud were brought to light after the public house boom of a few years ago. In the licensed trade the tenant is supplied by his brewer and distiller with a Pass Book in which is entered a copy of his account in their Ledger, and houses were freely bought and sold on the basis of the length of lease held by the licensee or vendor, together with his monthly payments to his brewer and distiller, this giving sufficient material to form a rough estimate of the value of the property. It was found that in several cases publicans had purchased and paid for goods in order to have them entered up in their Pass Books, but the goods were not sold on the premises but poured down the drain, the purpose of the vendor being served by having the goods entered up in his Pass Book. On the entry in the Brewer's Pass Book the vendor could claim having paid a certain sum per month to his brewer or distiller, upon which payment the goodwill of his property would partly be assessed.

OMISSION OF PURCHASES.—Frequently all purchases are entirely omitted from the books or entered at a date subsequent to the closing of the accounts, when the goods have been received prior to the close of the year for which the accounts are made up and taken into stock. Anything of this nature should, however, be immediately discovered, if any reasonable system of stock books were in vogue, and would probably be brought to light in the ordinary course of events, if sufficient time were allowed to elapse, but, as a rule, when accounts are prepared for the purpose of a prospectus or a sale, the time at the disposal of the staff is not very great, as it is always desirable to bring the accounts, upon which the sale is made, up to the very latest date.

Frauds of this category should, in theory, never materialise. The obvious inference is that the person who purchases a business without having the figures upon which the transfer is based, thoroughly investigated by an independent and capable party, is simply laying himself open to the wiles of the unscrupulous vendor. The professional accountant employed upon an investigation for this purpose would, as a matter of course, inquire into all the points above enumerated, and thus frequently save many individuals from losing the benefit of their industry. It is surprising, however, how many keen business men are willing to accept the statements made to them by vendors rather than pay for the expert knowledge which they have not had the training or experience to acquire.

In cases where the transfer of a business takes place, the books of which have been falsified in

order to cover up defalcations of which the vendors have no cognisance, it is possible that although the purchaser is buying on incorrect accounts, he need not of necessity suffer injury thereby. If, for instance, the manipulation of the accounts has taken place in the Profit and Loss Account either by the omission or understatement of income or the over-statement of expenses, this will probably only be done to the extent of the defalcations, in order that no glaring discrepancy shall appear in the accounts, as compared with those of previous years, and the net result is, therefore, the same as it would have been had there been no defalcations. If, on the other hand, the manipulations take place in the Balance Sheet, either by the understatement of liabilities or the overstatement of the assets, the former are frequently not taken over by a purchaser, but even should this be the case, the under-estimation should be discovered in the process of investigating the accounts, whilst, as regards the assets, it is unusual for these to be taken over except upon an independent valuation. The question of goodwill does not need consideration, as if this is arrived at by any scientific calculation at all, it will be a certain number of years' purchase of the profits, which, if in any way falsified, have been brought up to a reasonable standard by manipulation in order to cover the defalcations made during the period covered by the accounts.

NEGOTIABLE SECURITIES.—Frauds to which a certain class of employers are particularly liable are those in connection with securities of an easily negotiable nature. In businesses where financial operations of this nature comprise the greater part of the transactions, the principals must of necessity gather round them assistants in whom they are compelled to place the utmost confidence, and on them devolves the duty of handling a vast number of bearer securities. These assistants become familiarly acquainted with those with whom transactions are constantly in progress, and consequently they receive and act upon their instructions as readily as they would were they dealing with the principals themselves. As soon as such a state of affairs exists, the way is open for the assistant to commence fraudulent operations with his employer's property which must, in the course of time, lead to his downfall. It is in his power to sell any security that will serve his purpose and to commence such a series of substitutions that, in a very short period of time, the defalcations may aggregate to an amount that might bring ruin to the employer. Naturally frauds of this nature can be guarded against by a proper system of control and constant inspection, but where the system is in any way loose, the object in view can be rapidly attained, as dealings in securities are in the most part transactions of great value.

INFLATION OF STOCK.—Another means of fraud is by the manipulation of the stock of a trading or manufacturing company. Unless great care is taken, the stock may be brought in either in excess quantity or at a price in excess of the cost price of the raw material, plus any labour spent thereon, and in certain trades, possibly interest. Although accountants take no responsibility for the value at which stock appears in the accounts which they have audited, unless they have express instructions to do so, it nevertheless behoves them to exercise the utmost care as regards the checking, so far as within them lies, of this item in the Balance Sheet. Some very important actions have in recent years been decided upon this question of stock, in several of which attempts have been made to make the auditors of the company liable for the loss sustained, but generally speaking, it may be taken as settled that, in the absence of suspicious circumstances an auditor is not guilty of negligence who relies upon the statements made by trusted officers of a company. In the event, however, of any suspicion at all being created in his mind, it is the place of the auditor to probe the matter to the bottom.

The inflation of stock quantities and values is frequently a means of covering a default. It is possible that an employee, owing to lack of supervision, may be in such a position that he has complete control over the stock. It would be a perfectly easy matter for him to extract articles from the stock and sell them on his own account. In such a case it is generally found that this employee is relied upon to take stock at prescribed periods. It becomes necessary for him to cover his deficiency and, especially if the articles are at all numerous, he finds little difficulty in adding to his count a sufficient number to conceal the shortage. If this form of fraud were practised to any great extent, it would probably soon reveal itself in a comparison of the percentages of gross profits to net sales, but in any case it would be a difficult matter for an employee to continue the offence for a lengthy period, as the shortage of those stocks which he has appropriated should soon become apparent.

A further instance of manipulation of stocks may occur in a concern where the value of the merchandise dealt in is subject to market fluctuations. A very important part of such a business is judicious buying, and it is easily seen how considerable losses may arise during a financial period through speculations on the part of the responsible officials. To cover these losses the stocks purchased in a high market may have been taken in at cost in spite of the fact that a heavy drop has taken place in the value of the commodity with no prospect of recovery, or on the other hand, cheaply bought stock may be valued at its temporary high market value, thereby anticipating a profit that

may never accrue. Such methods for showing good results, or concealing losses are not invariably employed with actual fraudulent intent, but the effect of them, which the officials may not be in a position to foresee, may easily be the means of placing them in the awkward position of proving their innocence of a charge which the facts of the case would seem to imply. Under any circumstances, however, the effect of such over-valuation can only act in one way, and that is to recoil upon the succeeding period.

A fraud of a somewhat special nature is that which may be committed as between the active and sleeping partners of a firm or the partner in a firm who has control of the accounts, as against his co-partners, whereby it may be possible for him not only to defraud him or them, but also to defraud the creditors of the business. In such a case, if the responsible partner be so willing, and unless his co-partners keep a close watch on the details of the business, it is possible for him to inflate unduly the assets of the business, thereby himself drawing a larger share of the profits than he would be otherwise entitled, or possibly raising a large amount from creditors either on loan or in respect of goods, to which creditors, in order to obtain advances, he may possibly have had to show his Balance Sheet. On the other hand, the partner in charge of the accounts may intentionally return the profits of the business below what they should be in order to pay out his partners at a lower rate than they would be otherwise entitled to receive.

COST ACCOUNTS.—Cost Accounts are of a nature which lend themselves easily to fraudulent manipulation, especially so in the case where there are not a large number of persons employed upon the summarising of the details and keeping of the Costing Accounts. This is sometimes due to the somewhat illiterate class of person which is chiefly instrumental in preparing the original memoranda from which the Cost Accounts are eventually prepared. Where a large number of contracts are in hand at the same time, and where they extend over a considerable period, it is possible for the labour and materials used and employed upon an unprofitable contract shortly drawing to a close to be charged to some new contract which has only just begun, or upon which there are hopes of making a considerably larger margin of profit. In cases such as these, provided that the firm is continually obtaining new work, and the contracts are of a sufficiently large nature, it is comparatively easy to continue the manipulations between various contracts over a long period of time, but in these cases, as in most others, there comes a day of reckoning, when the manipulations in the accounts are brought to light, possibly by a slackening in trade, whereby an unusually large number of contracts are

terminated in a particular financial year, or possibly owing to a detailed investigation of the amount appearing in the Balance Sheet under the head of "Uncompleted Contracts on hand," owing, perhaps, to the large amount to which this asset had in course of time amounted to.

Another class of frauds is that in connection with executors and trustees. The obligations imposed upon such persons are usually of an onerous character and their liability, even for quite innocent neglect of duty, is often extremely heavy, therefore any breach in the performance of what is almost a sacred trust is the more to be deplored. Especially in the case of trustees, where the beneficiaries are perhaps only young children and the trust extends over a period of years, the trustee, if he is so disposed, frequently has it in his power to deprive the *cestui qui* trust of the whole of the estate. How often is it experienced that the capital of an estate has been misappropriated, the income in the meantime being paid, until the day arrives upon which the estate is to be handed over to those entitled to it. The great safeguard against such a calamitous state of affairs is to provide that the accounts of the trustee are subjected to periodical audit.

Somewhat akin to this class of fraud is the conversion to their own use by solicitors of moneys entrusted to their care. These cases are unfortunately of somewhat frequent recurrence, but it is satisfactory to note that apart from the action taken by the Law Society towards such of its members as transgress the law, the Courts regard this crime as particularly despicable, and mete out justice accordingly. So long as those in possession of means do not protect themselves against such frauds, there will always be found unscrupulous persons ready to take advantage when occasion presents itself.

CASHIER'S EMBEZZLEMENT.—The simplest examples of fraud are those which may be carried out by the cashier of a business, and particularly is this the case in small businesses where the cashier not only receives and pays cash, but acts as clerk also, because, acting in the dual capacity, it is easier for him to manipulate the books in order to cover his embezzlement of cash. In cases such as these, it is sometimes found that a cashier has passed through his Purchases Book and taken to the credit of a fictitious person in the Bought Ledger (often in a general account headed "sundry creditors") an amount in respect of which goods were neither ordered nor received by his employers, and the credit is made by the book-keeper merely to make good an amount which he has abstracted from the cash. This may also be cited as an instance of the bad principle involved in paying any accounts other than by crossed cheque, because if in the example referred to the cashier had created a fictitious credit which

he wished to clear by a payment, it would be far more difficult for him to obtain a crossed cheque, which would previously have had to be signed and scrutinised either by the partners in the firm or by the directors of the company employing him. Furthermore, if the cheque when presented for payment had been specially crossed or marked "not negotiable," it would have been still more difficult to negotiate.

PASS-BOOK ENTRIES.—A system of fraud that happily is not frequently resorted to owing to practical difficulties, is that whereby defalcations are concealed by means of a duplicate Pass Book and Paying-in Book. This would generally necessitate the crime of forgery in addition to that of embezzlement; but while such cases have occurred where control over the Banking Account has been left in the sole charge of the defaulting cashier, it seems inconceivable to imagine such a system could be successfully carried on for any length of time where an effective audit is in operation.

Tampering with the entries in a Pass Book is again a falsification which is fortunately not common. It might be possible for a cheque, say for £15, to be drawn on account of petty cash and entered as £5 in the Cash Book, the "1" in the Pass Book being subsequently erased. The £10 would then be paid in to cover an extraction of that amount from the receipts and an entry for a similar amount made in the cash column of the Cash Book on account of such an item as bill stamps, of which no record is kept. This would not, however, be a very fruitful source of embezzlement as a frequent recurrence of such an item would quickly give rise to suspicion apart from the great risk that would be run in erasing figures in the Pass Book.

Illustration of a fraud by means of erasing a figure in the Bank Pass Book referred to above.

CASH BOOK

	£	s.	d.		£	s.	d.
To A . . .	20	0	0	By Wages . .	15	0	0
" B . . .	5	0	0	" Petty Cash .	5	0	0
" C . . .	40	0	0	" Bill Stamps .	10	0	0
" D . . .	10	0	0	" H . . .	30	0	0
" E . . .	25	0	0	" K . . .	10	0	0
				" Balance . .	30	0	0
	£100	0	0		£100	0	0

BANK PASS BOOK

	£	s.	d.		£	s.	d.
To Cash . .	25	0	0	By Wages . .	15	0	0
" " . . .	40	0	0	" Cash . . .	15	0	0
" " . . .	35	0	0	" H . . .	30	0	0
				" K . . .	10	0	0
				" Balance . .	30	0	0
	£100	0	0		£100	0	0

The item cash £15 on credit side of the Pass Book, represents petty cash £5, and bill stamps £10, of which latter no record is kept. The "1" is erased after the Pass Book is totalled.

Frauds frequently also occur in regard to discounts, where a receiving cashier has either the control, or if not the entire control, the opportunity of inspecting and making entries in the Sales Ledger of a company. Instances occur where a cashier, having received a sum of money from a customer and given him a receipt for the full amount, enters the cheque on the counterfoil of the receipt for a smaller amount than actually received, and treats the difference between the amounts entered and received as a discount, thus being able to make good a sum or sums which he has previously misappropriated either in cash or by means of a cheque of equal amount.

There is also the simple misappropriation of cash by a cashier for which he gives a receipt out of a separate book kept for the purpose and not in general use, or a receipt which he has obtained by subterfuge, either by filling up a previous counterfoil and giving a blank receipt, or filling up two counterfoils and only giving one receipt, or possibly cancelling a counterfoil and not the receipt.

In the majority of cases of misappropriation by cashiers it is found that the defaulting party has devised some scheme whereby he thinks his defalcations can be systematically concealed. It will, of course, be apparent that if he is not in the position to cover up the fraud by passing through

entries in the shape of allowances for the amount of his deficiency, he must either resort to alterations of figures, or utilise a payment by one customer to balance the account of another which remains in debit owing to a previous extraction of cash. The former method is beset with difficulties, and unless he has access to the whole of the books, it is most unlikely to be adopted, consequently the latter is more generally resorted to in a more or less elaborate form. It naturally requires a particularly intimate knowledge of the various terms of credit extended to customers, and the methods by which they settle their accounts, and it is quite remarkable how far a carefully recorded system of fraud of this nature can be extended. But no system ever devised has been able to overcome the human element in the case, and it is here that the faulty link in the chain is frequently found. An illness overtakes the cashier, he meets with an accident, he may even receive promotion. The system cannot work unless he is there to control it. This is why it is essential to see that any person handling cash takes an annual holiday, and takes it all at one time.

The first item that has been manipulated is 5th Jan., C who has paid £50 on account. The cashier incorrectly credits him with £10 discount knowing that he will be shortly remitting again, which he does on 9th Jan., when he pays a similar amount, but the cashier pays in only £40, thus covering the £10 discount. C's account is credited with £100 in all and therefore remains in order.

Illustration of a Falsified Cash Book

(All Cash Receipts being retained for office use and only Cheques banked.)

			Discount			Cash.			Bank.						Cash.			Bank.		
			£	s.	d.	£	s.	d.	£	s.	d.				£	s.	d.	£	s.	d.
Jan. 1	To Balance					157	0	0	986	0	0	Jan. 2	By Wages		40	0	0			
" 2	" A	Cheque	4	4	0	80	0	0				" 3	" K					70	0	0
" "	" B	Cash		10	0	9	10	0				" "	" Petty Cash		10	0	0			
" 5	" C	Cheque	10	0	0	50	0	0				" 5	" Bank per contra		130	0	0			
" "	" Bank per contra								130	0	0	" 7	" M					98	0	0
" 6	" E	Cheque	50	0	0	950		0				" 9	" Bank per contra		1,025	0	0			
" 8	" F	Cheque				75	0	0				" 12	" Sundry Creditors		200	0	0			
" 9	" Bank per contra								1,025	0	0	" "	" N					475	0	0
" "	" C	Cash				40	0	0				" 14	" Bank per contra		339	3	0			
" 12	" G	Cash	4	15	0	90	0	0				" 17	" L, Contra a/c					95	0	0
" 14	" H	Cheque	16	0	0	313	3	0				" "	" Balance		46	10	0	1,837	3	0
" "	" D	Cheque	1	7	0	26	0	0												
" "	" Bank per contra								339	3	0									
" 17	" Contra a/c		5	0	0				95	0	0									
						£ 1,790	13	0	2,575	3	0				£ 1,790	13	0	2,575	3	0

In a Cash Book where large amounts of discount appear it is quite probable that the magnitude of this deduction may go unnoticed.

On 6th Jan. D pays cash £26 which the cashier misappropriates. It is shown here and ruled through for the purpose of illustration. This is covered by a manipulation in the Day Book. The invoice, not being copied, is subject to 5 per cent. for cash per return, and is rendered to H correctly on 12th Jan. It is entered in the Day Book thus—

170 doz. Articles at 42s. per doz.	£357	0	0
Less, 5 per cent. for cash	17	17	0
	<hr/>		
			£329 3 0

It will be noticed that there is an error in the deduction of £10, but this would scarcely be noticed in checking the posting. H remits by return per cheque £339 3s. 0d. The cashier credits him with £313 3s. 0d. and discount (roughly 5 per cent.) £16, so leaving £26 to be appropriated to D's account.

The item L is to settle as Contra Account. Lawes £100 and £95 is due to him, both being net. He pays £5 in cash to settle. The cashier treats this as discount, and makes a contra entry in the Cash Book—bank column—for posting purposes.

It will be seen that the whole of the receipts *shown* as cash have been accounted for and all by cheque have been banked.

COLLECTORS AND TRAVELLERS.—Collectors and travellers, where the latter also act as collectors, are in very much the same position as the cashier of a business, except that they have far more freedom of action, and spending their lives in an environment which may possibly lead them into a mode of living in excess of their income, are more susceptible to misappropriation of funds in their hands than is the cashier of a business over whom more control can be exercised. In such cases the best preventive is to pay the official a salary commensurate with his responsibility and insure him for the maximum sum which he is likely to have in hand at any time.

Where there is an absence of strict supervision, there is a large scope for fraud in connection with the accounts of branch shops and agencies, either by embezzlement of cash or stock, as of necessity the manager must have extensive powers. In certain businesses this is to some extent met by charging all goods to the branch at selling prices, the manager having to account for the same by cash, discount, book debts or stock taken on the same basis, the advantage of this system being that it obviates the necessity of keeping elaborate Stock Accounts. On the other hand, in some cases, goods are charged out to the branch at ordinary prices, and absolute reliance is placed on the manager until such time as the periodical accounts show unsatisfactory results,

when it is probably immediately assumed that the man must be either a fool or a rogue, and, neither being of any use to the proprietor, he is dismissed on the first opportunity.

Fraud very frequently occurs in the Wages Accounts of large undertakings, where in some cases the wages bill runs into several thousands of pounds a week. Sometimes names are duplicated, sometimes dead men remain on the wages list for a considerable period, and sometimes the frauds are due to merely arithmetical errors in the additions or extensions of the wages lists, or alterations in the lists after payment.

PREVENTION OF FRAUD.—Whilst it must be frankly admitted that it is impossible to prevent fraud, undoubtedly the very best means of providing against and minimising fraud in any business is the institution of a complete internal check upon the accounts, combined with an efficient audit. Provided that the system instituted is a full and comprehensive one, and that care is taken to see that it is rigorously carried out, no serious defalcations in any business should be capable of being carried on for any considerable length of time. This is neither the time nor the place to describe in detail an efficient system of internal check, the essence of which is a frequent change of clerks in each department, and that the work should be so distributed that, although each clerk should be held responsible for the accuracy of the entries in the book which he keeps, while no one else should make any entries therein, yet as many persons as possible should be concerned in each transaction. By these means no irregularities should go on for any length of time, except there be wholesale collusion. Unless these main principles form part of the scheme and the system is carried out in its entirety, it is better to be without any system of internal check, as a faulty system, or one not efficiently carried out, is worse than no system at all, as it is only delusive, as was evidenced a few years ago, when the Bank of Liverpool frauds were brought to light.

The system introduced must necessarily have regard to the staff employed, and that for a business employing a small number of clerks need not be so elaborate as that employing a large number as in the former instance it is usual for the principal to be able to give more personal supervision in the office than would be possible when a large number of clerks are employed.

No better example can be found of the danger that is run where there is a lack of proper control than that provided by slate clubs and societies of a kindred nature. As the end of each year draws near, when most of these clubs distribute their funds to the members, one can scarcely pick up a newspaper without finding that the members of some society or other have been defrauded by a dishonest treasurer or secretary.

Part of the fault, no doubt, is to be found in the fact that so many of these societies are controlled by people of no financial stability, but there would not be the temptation to take the mean advantage of their fellow men if there existed the least shadow of control over their actions. And even where there is some attempt to subject the accounts to an audit, those whose duty it is to undertake the task invariably have not the remotest notion of what they are required to perform, and are accordingly likely to assist the defaulter by passing his irregularities rather than prevent him from accomplishing his ends.

Since the majority of cases of fraud are in connection with cash, it is most essential that every possible means of control over it should be utilised. The object to be kept in view being to spread responsibility over as many officials as possible where cash is concerned. The correspondence should be opened by some person other than the cashier, and all cheques, money orders and postal orders should at once be stamped with the crossing stamp of the company (or firm). Before the remittances are handed over to the cashier they should be entered in a Counter Cash Book, so that the General Cash Book can be compared with it. Where the staff is sufficiently numerous a separate clerk should make out the receipts, and again others be employed in making up the Bank Paying-in Book. The Bank Pass Book should be checked regularly by some person other than the one whose duty it is to write up the Cash Book. It is preferable, also, that the petty cash be not kept by the chief cashier, neither should he have anything to do with making up the wages, his duty, in this respect, simply being to pay the amounts according to the book prepared for him. If such points as these are considered and a system drawn up accordingly, it becomes a difficult matter for any one employé to tamper with the cash. A practice that should be discouraged, though it would be difficult to make it a hard and fast rule, is that of cashing cheques on behalf of customers and others. It is a practice that may easily be abused, and may even be the point at which defalcations first germinate.

SYSTEM OF INTERNAL CHECK.—The following are a few general principles to be borne in mind in connection with a system of internal check—

(1) Each day's takings to be paid to bank in full, without any deduction, on the day received.

(2) No payments to be made out of the daily receipts under any circumstances whatsoever.

(3) All payments to be made by cheque, and in the case of very small amounts, one cheque to be drawn for the specific purpose of paying several such small amounts.

(4) All cheques to be "specially" crossed and signed by a partner in the case of a firm, or by two

directors and the secretary in the case of a company, and no cheque to be signed unless the invoice for goods delivered or services rendered, or a monthly statement in respect thereof duly checked and certified is attached thereto.

(5) The cashier of the business not to have the control of any of the ledgers, either Bought or Sold.

(6) The Discount Book (if a separate book is used) to be kept by some person entirely independent of the ledger-keeper and cashier, and to be periodically perused by some person in authority. If discounts allowed are entered in the Cash Book then the discount column should be periodically examined by a responsible person.

(7) The Returns Book (both Bought and Sold) and Journal to be kept by some person independent of the cashiers and book-keepers, and to be periodically produced to and perused by some person in authority.

(8) Invoices for purchases to be checked with the carbon copy or counterfoil order given therefor, and not to be put forward for payment with cheque attached until it has been certified as accurate and complete in all particulars by the responsible person, viz.: (a) Calculations correct, (b) goods ordered, (c) goods received, (d) entered in Stock Book.

(9) The ledgers to be kept on the self-balancing principle, and totals as well as the balances to be agreed at periodical intervals.

(10) Full Stock Accounts to be kept and agreed, with periodical independent stocktaking, subject to reasonable allowances for "shorts," "breaking down," etc.

(11) The keeping of detailed Cost Accounts for each job in businesses when actual work is done as apart from merely turning over made-up goods (*i.e.* retailers and middlemen).

(12) An efficient system for the payment of wages.

The main point to be borne in mind in drawing up a system of internal check for any particular business is to consider where fraud is most likely to creep in, and then, having this in mind, to endeavour in the system to raise every possible barrier against its introduction.

A very useful preventive against fraud is that provided by numbered receipt books. In fact, it is a method that should be adopted by all business houses. But like all other checks, unless it is thoroughly organised and rigidly carried out, it is little more than useless. A register should be kept of all books printed. These should be kept under lock and key and issued in numerical order, the register being marked to who and on what date issued. The old book should be produced before a new one can be obtained. The unused books should be checked with the register at frequent intervals. All spoilt or unissued receipts

should be attached to the corresponding counterfoil. The counterfoils should be checked with the Cash Book, in which it may be found convenient to provide a column for the number of the receipt. Where there are a number of books in use, as for example in the hands of travellers and collectors, it should be arranged that each person has two books, so that every week one is at the head office for checking purposes. It is the custom in some houses to regard receipts issued by travellers as non-official, a confirmatory acknowledgment being sent direct. This is practically only a duplication of labour, and so long as it is stated that only the printed form of receipt is recognised, and the above-mentioned system of checking collections is in operation, there does not appear to be any great advantage in it, especially if statements are sent from head office with a request to communicate only with head office regarding any errors in the account.

The printed form of receipts that are frequently issued with cheques are a likely source of danger. They are certainly most useful for filing purposes, but in the hands of an unscrupulous cashier may cost a sum far in excess of that gained by the saving of time effected by the easy reference.

EXAMINATION OF BOOK DEBTS.—A detailed examination of the book debts should be made periodically, notwithstanding the fact that the balances of the ledgers may agree with the total of the particular Ledger Account. This is especially to be borne in mind in the case of very large companies and where there are charges accrued and debited and frequently payments in round sums are made on account. When checking the schedules of balances, care should be taken to scrutinise these as to any prolonged period over which these have considerably increased, and if this has been the case, a full investigation of the accounts should be made, both as regards the Personal Accounts and the corresponding "Charges Accrued" Account. Had this been done, the Millwall Dock Fraud would never have assumed the proportions which it did. At least a representative number of Ledger accounts should be scrutinised, especially as to the credit side, and authority should be produced for the writing off of bad debts and exceptionally large allowances and the making of transfers.

In dealing with book debts, attention should be given to accounts where it is found that there are debit cash items with no corresponding credit, and in particular, where there are officials who have personal accounts in the books against which are charged, as frequently happens, items in respect of drawings, expenses incurred on the employer's behalf, and often, amounts that have to be specially accounted for. All these debits require careful scrutiny, as defalcations sometimes are concealed in this manner. This is the case also

in the Drawing Accounts of principals. These gentlemen are not always too careful over their personal affairs, and it may be an easy matter for charges to be made to them for money which they have never received. It is always desirable that they should periodically investigate the charges to their accounts, but there seems to be a somewhat general disinclination to do so.

The verification of book debts of certain trading concerns requires special caution. In the majority of businesses, the debit entries are varying amounts, and usually a periodical settlement is made, but in the case of property companies, the debit entry for rent is usually the same, and in connection with these, care must be taken to see that one quarter's rent is not used to make good a previous quarter's rent previously misappropriated. For this reason the arrears of rents in a company of this nature should receive careful scrutiny.

Again, in the case of breweries and distilleries, although the charges for goods continually vary, it is the custom for the tenant to pay a certain round sum each month, and frequently this is fixed when he enters upon his tenancy. For this reason the cash payments should be tested in order to see if any payments by the tenant are missed. It should be borne in mind that in the liquor trade it is customary to make payments on the basis of lunar months, thus making thirteen payments per annum.

It is a growing practice with many large businesses to send out half-yearly "rest" statements, informing the customer of his balance and asking him to immediately communicate with the firm in the event of there being any inaccuracy in the same. It is unfortunate that this system is not more general, but in the case of a suspicion of fraud, it should always be acted upon at once, care being taken that some person having no connection whatever with the ledger clerk is deputed to send out the statements. In businesses where customers are supplied with Pass Books, it is well to have the Pass Books called in and examined with the Ledger Accounts at uncertain intervals, in order to see that they are in agreement therewith.

One of the best checks upon the correctness of the stock of a business is the comparison of the gross profit and the percentage of each individual item comprised in the Trading Account over a period of years, subject, of course, to any fluctuations due to increased cost of raw material, etc. In addition, the totals of the stocks at each balancing period should be compared to ascertain that the stock is not a continually increasing item, unless increased trade or special conditions justify it. Where possible it is also wise to fully trace a few invoices for goods received with the sales made in respect thereof, and see if the percentage of profit shown thereon is at all comparable with the

percentage of gross profit shown in the Trading Account. Wherever possible Stock Books should be instituted, and these should be kept in as detailed a manner as possible, and should agree with the independent stock-taking made at the close of each financial period. The periodical stock-taking should, of course, be made by some person entirely independent of the stock-keeper, and then the figures checked with the amounts shown in the Stock-keeper's Ledger, and any discrepancy should be most carefully gone into and explained. Although, after making allowances for small shorts, etc., the stock-taking may agree with the Stock Books, it is very important that the periodical schedule of stock should bear a certificate stating that "The foregoing stock is all good, saleable stock, is the property of the company (or firm), and has been taken at cost price or under if necessary." This certificate should be signed by the stock-taker, and also by the head of the business. The object of this certificate is to ensure as far as possible, in addition to the arithmetical accuracy of the quantity of the stock, that no old unsaleable stock is included, and also that, in the case of a business dealing in stocks which fluctuate considerably in value, that the stock has been taken either at cost price or at the market price of the day on which the accounts were closed, the lower of the two prices being the correct one to adopt for the accounts.

BUSINESS EXPENSES.—Similarly, a careful comparison of the expenses of a business with those of corresponding periods should be made, as it is in this way that attention is very frequently drawn to increases in expenses which are not legitimate, and may then cause the first suspicion of fraud and, upon investigation, lead to its discovery.

On the other side of the account the reasons for the fluctuation, and especially the falling off of sales, etc., and sundry items of receipt, should be investigated, in order to see that there is no leakage in income.

Care should also be taken that as many persons as possible are employed in preparing the wages sheets, in order to avoid collusion as far as possible, and if it cannot be entirely avoided, at least to provide that as many persons as possible are implicated therein. For this reason the time sheets or particulars of piece-work done should be certified by the foreman under whom the wage-earner is working, these should be listed by one set of clerks, the wages priced out by another set, and when these have been checked and the total amount of the wages ascertained, the payment should be made by an entirely different staff, a cheque for the exact sum total of the wages having previously been drawn. Before payment the whole of the amount of wages should be made up in tins or bags, each one marked with the employee's

number, and at the end of the day, the amount unclaimed should be taken charge of by the cashier until such time as the rightful owner applies for it. In the interim, the unclaimed wages should be repaid to bank, as in some undertakings the amount unclaimed amounts to a considerable sum. It is well at uncertain intervals for some entirely independent person to be present at and witness the pay, in order to act as an additional check on the staff, and in the case of certain undertakings, such as collieries, it is frequently the case for a representative of the auditors to be present at an occasional pay, in order that he may satisfy himself, so far as possible, that there is no fault in the system of pay adopted by his clients.

"OCCASIONAL" RECEIPTS.—Frequently defalcations take place in regard to the "occasional" receipts of a business. Under this head would come (a) transfer fees, (b) agreement fees and receipts for dilapidations and repairs in a property company, (c) dividends received in respect of bad debts subsequent to the whole of the debt being written off the books, (d) interest and dividends on investments, (e) sundry rents in a trading or manufacturing company, (f) duty drawback in the liquor trades, (g) sale of packing cases, (h) waste products and many others which might be enumerated. As regards all these, accountants have their own tests, which they make periodically, but a capable manager of a business should be able to keep control over them from his own knowledge of the particular business. A useful means of tracing income of this nature, which may have gone astray after receipt, is an occasional comparison of the Bank Paying-in Book with the Pass Book, as sometimes uncertain receipts of this nature received by cheque are paid into the banking account of the business in order to make up wholly or in part previous defalcations.

Whilst the Cash Book is generally the place where fraud will be discovered if it exists, every book in use is capable of falsification and should receive sufficient examination to satisfy the correctness of the entries contained in it. As an example, the Journal may quite possibly be utilised to record entries to cover misappropriation of cash, and in the way of passing allowances writing off so-called bad debts and the like, and through this book transfers may be made which will have the effect of altering the appearance of the accounts in general, and such entries may be so cleverly created that only the closest inquiry would elucidate their true purpose. The Sales Day Book, also, may contain items of a capital nature such as machinery sold which, if not detected, might serve to convey a satisfactory trading result, and at the same time preserve the book value of the asset. And again, recent experience has once more shown how the Share Registers

of a company may be falsified to such an extent as to create a state of affairs involving the theft of no inconsiderable sums of money at the expense of the unsuspecting shareholders.

For the purpose of detecting fraud no hard and fast rules can be laid down, nor would it be desirable. The foregoing paragraphs, however, provide many suggestions to that end, but it is by no means contended that their adoption "in toto" would necessarily disclose what it is sought to conceal. It might almost be said that no two sets of books are identical, and what might prove a very fruitful course of investigation in one case may be quite the reverse in what, at first sight, appears an exactly similar proposition. While there are brains of varying quality and capacity engaged in fraud and falsification, so will methods vary accordingly, and the means employed to detect the wrong must be adjusted to meet the particular circumstances. As new situations arise, so must they be met, but it is believed that the ideas conveyed, if acted upon, would do much to minimise the risk that is daily run by those who regard such organisation as a mere waste of time and money.

At this point it might be noted what an incomplete idea of an auditor's duties is held by so many laymen. Their conception of this work often seems to be that of ticking, casting and searching for fraud, in fact the last-mentioned strikes them as being the main object for which they are employed. Whilst the auditor should, of course, be always on his guard against anything of this nature, and should unceasingly watch for weak points in the system of book-keeping which would lend themselves to misuse by an unscrupulous employee, it is most decidedly the wrong principle to approach an auditor on the assumption that every member of the staff should be mistrusted from the outset. The auditor who enters upon his duties with this sole object in his mind would indeed be a most undesirable person to have in one's midst.

CONCLUSION.—Whilst it is generally admitted that so long as human nature is what it is, so long as ambitious persons desire to attain their ends by too speedy and illegitimate means, so long as the slothful desire to place themselves in the position of the industrious without going through the necessary preparation and years of work that the latter have had to undergo, so long will there be some inducement for the unscrupulous and clever to commit fraud and falsification for a time, a course of conduct which often seems to the uninitiated to be fostered by the judiciary when comparison is made between the altogether inadequate punishment meted out in connection with many frauds, when prosecution and conviction has followed, and the heavy penalties inflicted in connection with many minor offences. In the

long run, however, whatever may be the nature of the fraud, the probabilities are that it will eventually come to light, to the discomfiture and social ruin of the perpetrator, whether he be proceeded against, or whether he be treated with that generous compassion which is one of the brightest features of modern commercial life.

FRAUDS, STATUTE OF.

This celebrated statute, probably better known, by name at least, than any other Act of Parliament, was passed in 1677, and it still remains one of the keystones of English law. Its professed object was the requirement that certain transactions should be evidenced by writing to make them enforceable in a court of law, in order to act as a preventive against fraud and perjury. How far it has attained that end and how far it has failed to accomplish it is a much debated point.

The earlier part of the statute deals with conveyances and leases of land, and in combination with the provisions of the Act to amend the Law of Real Property, 1845, the law may be summed up as follows, namely, that leases for more than three years, and those for a less period when the rent is not equal to two-thirds of the annual value of the land, must be by deed, and so must all assignments, grants, and surrenders of leases, even though the leases themselves might have been created by parol. A lease for three years or less may be made by word of mouth if the lessee goes into possession at once; but if there is only an agreement for a lease, this must be evidenced by writing in order to be enforceable, in accordance with the terms of the 4th Section of the Statute of Frauds, which will be noticed directly. Although it was no doubt intended that all interests in real property should be brought within the scope of the Act, an exception has been held to exist in the case of an equitable mortgage (*q.v.*).

As to trusts, the Statute of Frauds provides that "all declarations or creations of trusts or confidences of any lands, tenements, or hereditaments shall be manifested and proved by some writing signed by the party who is by law enabled to declare such trust, or by his last will in writing, or else they shall be utterly void and of none effect." Any trust as to personal chattels, however, may be created by parol, provided it is to take effect in the lifetime of the creator of the trust. But a transfer of any trust must be evidenced in writing. The sections relating to wills have been repealed and re-enacted by the Wills Act, 1837.

The fourth section of the statute is as follows: "No action shall be brought whereby to charge any executor or administrator upon any special promise to answer damages out of his own estate;

or whereby to charge the defendant upon any special promise to answer for the debt, default, or miscarriage of another person; or to charge any person upon any agreement made in consideration of marriage; or upon any contract or sale of lands, tenements, or hereditaments, or any interest in or concerning them; or upon any agreement that is not to be performed within the space of one year from the making thereof; unless the agreement upon which such contract shall be brought, or some memorandum or note thereof, shall be in writing, and signed by the party to be charged therewith, or some other party thereunto by him lawfully authorised."

Here it will be noticed that there are five special kinds of contracts which are required to be evidenced by writing. The first and second are dealt with more especially under the head of GUARANTEE (*q.v.*); the third refers to any agreement to be executed in consideration of a marriage, but does not mean a promise to marry, which upon satisfactory evidence can be proved without any written document being in existence. The fourth shows the importance of having written evidence whenever an interest in land is concerned. There are many cases in which very fine distinctions have been drawn between what are and what are not interests in land; but it is unwise to rely upon these exceptions. If a person wishes to be secure he should never enter into any agreement which has anything to do with land or an interest in the same unless he justifies his position by some document signed by the person who is to be charged. The fifth kind of contract, that is, any agreement not to be performed within a year, refers only to those contracts which cannot, according to their provisions, be wholly performed within a year.

Though so much stress is laid upon evidence in writing, it is to be remembered that it is not any particular formal document that is required. Any note or memorandum is sufficient provided that it complies with the following points: It must contain the names of the parties, it should set out the subject-matter of the contract; it should also name the consideration (unless in the case of a guarantee); and it must be signed by the party to be charged or by his duly authorised agent. Many nice and interesting points have arisen as to the sufficiency of the memorandum or note which can be utilised for the purpose of providing the requisite evidence in writing, but sufficient has been said to indicate what is essential, and it is useless to enter into details as to the exceptions which may arise.

The memorandum of agreement, or any agreement made under hand only, and not otherwise specifically charged with duty, must be stamped with a sixpenny stamp. An adhesive stamp may be used, but it must be cancelled by the person

first signing the agreement. Fourteen days after execution are allowed for the stamping of an agreement under hand, and such post-execution stamping must always be by an impressed stamp. The following agreements are exempted from stamp duty—

(1) Where the subject-matter is of less value than £5, or is incapable of pecuniary measurement.

(2) Where the agreement has reference to the hire of any labourer, artificer, manufacturer, or menial servant.

(3) Where the agreement is one relating to the sale of any goods, wares, or merchandise.

The seventeenth section of the Statute of Frauds has been repealed and re-enacted, with amendments, by Section 4 of the Sale of Goods Act, 1893 (*q.v.*). The sixteenth section is replaced, with variations, by Section 26 of the same Act.

The contracts which are included in Section 4 of the Statute of Frauds are neither void nor voidable, because there is no evidence in writing of their existence. They are merely unenforceable by action. A defendant in an action at law must specially plead the section in his defence, otherwise he will not be heard as to any objection he might have raised against the action being brought on the ground of the want of statutory proof of the contract.

FRAUDULENT CONVEYANCE.

A conveyance of property for other than a valuable consideration made within a certain time before the bankruptcy of the person who executes the same. Thus, if a person makes a voluntary conveyance within two years before his bankruptcy, this conveyance is held to be fraudulent and therefore void under all circumstances. And even if the voluntary consequence has been executed within ten years before his bankruptcy it is likewise void unless the bankrupt can prove that he was quite solvent without taking into account the property comprised in the conveyance. The law as to fraudulent conveyances is contained principally in Section 42 of the Bankruptcy Act, 1914.

FRAUDULENT DEBTORS.

Under Section 154 of the Bankruptcy Act, 1914, there is provision made for dealing with debtors and bankrupts (whether discharged or not) who deal or who have dealt with their property in such a manner as to prejudice their creditors and so to defraud them. It would be impossible to go through all the offences enumerated in the section in detail, but a summary of them may be given by stating that the matters dealt with—and most of which are punishable with imprisonment up to two years as a maximum—are (1) failure to make a full discovery of property, (2) failure to deliver up property, (3) failure to

produce books, (4) concealment of property, (5) removal of property, (6) omissions in statements of affairs, (7) failure in disclosing fraudulent claims on the estate, (8) concealment, mutilation, or falsification of books, (9) obtaining credit by false representations, (10) fraudulently carrying on business, and (11) fraudulently pawning or pledging property obtained on credit. Under the former law it was for the prosecutor to prove any of the above offences, if they were alleged against the debtor; now the burden of proof is shifted, and it is for the debtor to show that his dealings with his property were not of a dishonest character.

Closely connected with fraud are various other offences set out in the Bankruptcy Act, 1914, on conviction for any of which a debtor may be imprisoned. They are gambling, failing to keep proper books, absconding with property, and obtaining credit whilst being an undischarged bankrupt, to the extent of £10 or upwards, either alone or jointly with any other person, without disclosing the fact of the bankruptcy to the creditor. It is also a criminal offence for an undischarged bankrupt to engage in any trade or business under a name other than that under which he was adjudicated bankrupt, without disclosing to all persons with whom he enters into any business transaction the name under which he was adjudicated bankrupt. (See also *BANKRUPTCY ACCOUNTS*, p. 177.)

FRAUDULENT PREFERENCE.

This signifies the payment by a debtor to some one or more of his creditors with a view of putting him or them in a more favourable position than the rest of his creditors. By Section 44 of the Bankruptcy Act, 1914, it is enacted—

(1) "Every conveyance or transfer of property, or charge thereon made, every payment made, every obligation incurred, and every judicial proceeding taken or suffered by any person unable to pay his debts as they become due from his own money in favour of any creditor, or any person in trust for any creditor, with a view of giving such creditor or any surety or guarantor for the debt due to such creditor, a preference over the other creditors, shall, if the person making, taking, paying, or suffering the same is adjudged bankrupt on a bankruptcy petition presented within three months after the date of making, taking, paying, or suffering the same, be deemed fraudulent and void as against the trustee in the bankruptcy.

"(2) This section shall not affect the rights of any person making title in good faith and for valuable consideration through or under a creditor of the bankrupt."

It will be seen that the section (as an amendment upon the Act of 1883) brings in as fraudulent a

preference to a surety for the bankrupt's debt to a bank. If a debtor pays off the debt and becomes bankrupt within three months the trustee will require payment of the money; and if money belonging to the debtor's estate is used to release a surety, the trustee will call for that money, and in the meantime the banker will have cancelled, or given up, the guarantee he held for the security.

The doctrine of fraudulent preference has become extremely technical, and although in a general way it is easy to see what is aimed at, it is not always so simple to bring the matter home to the person charged. In any case it is to be observed that the consequences must be entirely voluntary, otherwise no fraudulent intent will be presumed. The burden of proving that a preference is fraudulent is always on the trustee in bankruptcy.

Fraudulent preference arises in the case of the winding up of a joint stock company as well as in the bankruptcy of individual persons. By Section 210 of the Companies (Consolidation) Act, 1908, it is provided—

"(1) Any conveyance, mortgage, delivery of goods, payment, execution, or other act relating to property which would if made or done by or against an individual be deemed in his bankruptcy a fraudulent preference, shall, if made or done by or against a company, be deemed, in the event of its being wound up, a fraudulent preference of its creditors, and be invalid accordingly.

"(2) For the purposes of this section the presentation of a petition for winding up in the case of a winding up by or subject to the supervision of the Court, and a resolution for winding up in the case of a voluntary winding up, shall be deemed to correspond with the act of bankruptcy in the case of an individual.

"(3) Any conveyance or assignment by a company of all its property to trustees for the benefit of all its creditors shall be void to all intents."

FREEHOLD PROPERTY.

Although the name freehold property is most commonly applied to estates in fee simple, that is, those estates in which the holders have, as far as the English law will allow, an absolute property and can dispose of them almost exactly as they please, by conveyance or will, estates of a less degree are equally entitled to the name of freehold. Thus, a tenant for life or a tenant in tail has a freehold, but when the holding is for a limited period, as under a lease, the estate is not one of freehold. The name appears to be derived from the fact that the person who holds the estate holds it direct from the Crown, and that the estate was formerly held on services that a *free* man

could perform. In almost every case, whatever services were once due to the Crown have been terminated. (See also AUDITING, pp. 91 and 96; BALANCE SHEET, p. 144.)

FREEHOLDS, DEPRECIATION OF.

(See RENEWALS AND DEPRECIATION.)

FREIGHT.

(See TRADING ACCOUNT, p. 918.)

FRIENDLY SOCIETIES.

These are societies which are formed for the benefit of the members of the same during periods of illness, in old age, and for the assistance of the widows and orphans of the members, and also for other similar purposes. These societies are governed by various statutes, the principal of which are the Friendly Societies Act, 1896, the Collecting Societies Act, 1896—which has, however, only a modified application—and the Friendly Societies Act, 1908. It was the scandal so often mixed up with societies of a mutual benefit character that led to the introduction of legislation upon the subject, and consequently it is to the Acts of Parliament themselves that reference must be made in order to learn the various rules which are applicable to these combinations. All friendly societies are now supervised by a central office, with a chief registrar and assistant registrars, and this office prepares forms, approves rules, publishes statistics, and generally controls the working of the Acts. The rules are the basis of everything connected with the working of the society in every detail, and these alone can give full information as to the rights and benefits to be enjoyed by the individual members.

FRIENDLY SOCIETIES, APPOINTMENT OF AUDITOR OF.

(See AUDITING, p. 60.)

FRIENDLY SOCIETY, AUDIT OF.

(See AUDITING, p. 67.)

FUEL : EXPENSES OF.

The cost of fuel is a manufacturing expense, and the balance of the account, after being credited with the stock of fuel on hand, should be charged against the Manufacturing Account.

The outlay on fuel should bear a fairly constant ratio to the output of manufactured stock, and this fact enables the auditor to make an additional test of the accuracy of the charge. It is necessary in applying the test to take into account the rise and fall in prices of fuel. Consequently, the test would be more effective if applied to the *quantity* of fuel consumed, rather than to the value. Where there is no direct relation between the fuel consumed and the output, then the cost or quantity consumed "per week" may be compared for checking purposes.

FULLY SECURED CREDITORS.

(See BANKRUPTCY ACCOUNTS, p. 161.)

FUNDING.

The Government is often compelled to raise money for immediate purposes and this is done by means of Treasury Bills and Exchequer Bonds, which are repayable at stated periods. They form what is sometimes called the "floating debt" of the country. If, however, this floating debt is changed into a permanent debt, like consols, upon which interest is paid in perpetuity and the principal is no longer redeemable at a stated date—although, of course, the new securities are always transferable—the process of change is known as "funding."

FUNERAL EXPENSES.

(See EXECUTORSHIP ACCOUNTS, p. 449.)

FURNITURE, FIXTURES, &c.

(See BALANCE SHEET, p. 147; DEPRECIATION; also RENEWALS AND DEPRECIATION.)

FUTURE BOOK DEBTS.

Accounts which will in the future be due to the owners, owing to the carrying on of their business.

GARNISHEE ORDER.

THIS is an order granted by the court commanding a person who is a debtor of a judgment debtor not to pay over the amount of the debt which is owing to the judgment debtor, the object of the same being to prevent the judgment debtor from obtaining the money and applying it to his own use instead of paying the same to his creditors. The procedure is first of all to obtain a garnishee order *nisi*, which will be granted *ex parte* upon a good *prima facie* case being made out, and when this order has been served, the debtor of the judgment debtor is restrained from paying over the amount of the debt, or dealing with the money owing in any way. The person against whom the order is made is called the "garnishee." Afterwards, when the order *nisi* is made absolute, which will follow in due course unless the debtor can show good cause why it should not be made, the creditor who has obtained the order is entitled to receive the amount of the debt owing, and the garnishee must either pay the same into court or submit to an execution being levied upon his goods and chattels for the same. Payment by the garnishee to the execution creditor is a good discharge of the debt which was owing, or of that part of it which is actually paid if the total amount of the debt owing by the garnishee is greater than the debt of the execution creditor.

A garnishee order is not valid against the trustee in bankruptcy of the judgment debtor, unless completed by receipt of the debt before the date of the receiving order and notice of the presentation of a bankruptcy petition by or against the debtor, or the commission of an available act of bankruptcy by him.

The following are not available for attachment—

- (1) Unliquidated damages due to a judgment debtor.
- (2) Money due to a shareholder in the voluntary winding up of a limited liability company.
- (3) Purchase money payable upon the completion of a sale of real property.
- (4) Wages due to a seaman, servant, labourer, or workman.
- (5) Future income of a tenant for life.
- (6) Salary accruing but not actually due.
- (7) The pay or pension of an officer.

GAZETTE NOTICE.

A notice contained in the *Gazette*, the official organ of the Government, a periodical which is

published twice a week, on Tuesdays and Fridays. In a court of law, the production of a copy of the *Gazette* is, generally speaking, evidence of any notice or order contained in it.

In addition to the official notices of the Government, this publication contains advertisements as to all the principal steps taken in bankruptcy, winding up of companies, changes of partnerships, and notices calling upon creditors and others to come in and prove their claims in the administration of estates.

GENERAL AGENT.

A general agent is one who has authority conferred upon him to do anything which comes within the limits of the position in which he has been placed by his principal. In this way a general agent occupies a position which is intermediate between that of a special agent, whose duties are strictly limited, and a universal agent, whose duties are altogether unlimited. An example of a general agent is that of a person who is placed in management of a house of business, when he has an implied authority to bind his principal by doing anything which comes within the ordinary scope of the business. (See also AGENT.)

GENERAL BALANCE SHEET.

(See DOUBLE ACCOUNT SYSTEM, p. 421.)

GENERAL LEDGER.

A Ledger kept for the reception of all accounts, except those of the Bought and Sold Ledgers, and, therefore, containing the Nominal Accounts, Private Accounts, and probably Bills Receivable and Bills Payable Accounts. The General Ledger is usually completed by the inclusion of Adjustment Accounts for the Bought and Sold Ledgers, and it thus contains full particulars from which Final Accounts may be prepared, and gives the key to the position of the business at any time. Whatever subsidiary Ledgers may be kept, the information required for this purpose may be condensed in one Ledger by means of the transference of totals, and this Ledger is the one in any particular case known as the General Ledger.

GENERAL LEGACY.

(See LEGACIES.)

GOING CONCERN.

A concern in operation. The expression is also used in reference to the sale of an undertaking without any stoppage of business.

GOOD CONSIDERATION.

Any consideration for a contract which is founded entirely upon love and affection or some personal connection, instead of upon something which the law considers valuable, such as money or something which can be estimated in money. (See CONSIDERATION.)

GOOD FAITH.

This implies, both in law and in ordinary usage, an absence of anything which has about it a tinge of dishonesty, fraud, deceit, wilful misrepresentation, or a suppression of the truth. It is a necessary element in the formation of all ordinary contracts, and when spoken of in a general way the Latin words *bona fides* (with its ablative *bonâ fide*, "in good faith") are most commonly used instead of the English expression. In certain statutory enactments, however, particularly the Bills of Exchange Act, 1882, and the Sale of Goods Act, 1893, the words "good faith" are invariably found, and in each of the Acts just named it is stated that "a thing is deemed to be done 'in good faith' within the meaning of this Act when it is in fact done honestly, whether it be done negligently or not." The opposite of "good faith" is "bad faith," the Latin words being *mala fides* (with the ablative *malâ fide*, "in bad faith.")

In contracts of insurance something more than good faith is required. There is needed what is known as *uberrimae fidei* (*q.v.*).

GOODS.

The particular commodity dealt in by a concern in the ordinary course of carrying on its business, usually applied only in reference to trading concerns.

GOODS ACCOUNT.

An account to which purchases, sales and returns (both inward and outward) are posted, sometimes by totals from the books of original entry, but often in detail, for each transaction. The account commences with the stock brought down from the previous period, and is credited with the stock at the end of the period, and hence its balance represents the gross profit. (See also BANKRUPTCY ACCOUNTS, p. 177.)

GOODS IN TRANSIT.

The treatment of goods in transit in the books of account depends on whether the invoices for such goods have been brought into account. If the invoices have been included as charges against the period's trading, then the goods in transit must be included at their invoice value in the stock on hand. Otherwise, the goods in transit may be ignored for Balance Sheet purposes.

Where goods in transit are included in the stock on hand, the auditor must satisfy himself that the invoices in respect of them are charged in the accounts, and that the goods are not over-valued in the stock. For this purpose the auditor will have to examine and compare the Goods Received Book and the invoices, particularly those charged towards the end of the period. His examination is considerably facilitated where there is in existence a system of cross reference between the Goods Received Book and the invoices, the former bearing the number of the invoice and the latter bearing the folio of the Goods Received Book. This serves the double purpose of drawing attention to the inclusion of invoices for goods in transit, and the omission of invoices for goods actually received. (See also BRANCH ACCOUNTS, p. 265.)

GOODS ON APPROVAL.

Where a considerable quantity of goods are sent out on "sale or return," it is advisable that a separate Day Book should be provided for recording these transactions. The book should be ruled so as to avoid the necessity of posting to the Ledger any transactions other than those which become absolute sales. For this purpose the book should be tabulated so that goods forwarded may be first recorded at the date of dispatch, and that the ultimate fate of these goods (*i.e.* sale or return) may be subsequently recorded on the same line in the columns following, as shown on opposite page.

The register should be balanced across periodically, the total of the "Goods sold" column being credited to Sales Account. The outstanding items should be closed off by transferring them to a new portion of the register, where they will form a list of the stock of goods out on approval.

In dealing with goods on approval, the auditor should take particular care that only actual sales are taken credit for, and should observe that a proper reserve is made upon the stock of goods out on approval at the end of a financial period, in respect of "loading of profit" contained in the invoiced prices, so as to reduce the value of the stock to cost price. (See also ADJUSTMENTS AT BALANCING TIME; INVESTIGATIONS, p. 576.)

GOODS ON HIRE PURCHASE.

(See AUDITING, p. 95.)

GOODS ON APPROVAL REGISTER

Goods sent out.			Goods returned.			Goods sold.		Balances transferred.	
Date.	Particulars.	Amount.	Date.	Particulars.	Amount.	S.L. fo.	Amount.	New Register Fo.	Amount.

Only the items appearing in the "Goods sold" column are posted to the Ledgers.

GOODWILL.

The term "goodwill" is in constant commercial use, but its meaning is obscure, and the nature of the value which the word represents is often misunderstood. Goodwill has never been very satisfactorily defined.

ANCIENT USE OF THE TERM "GOODWILL."—The word "Goodwill" has been in commercial use for centuries, as is shown by the following references to old writers—

"1571. Wills & Inv. N.C. (Surtees 1835) 352. I gyue to John Stephen . . . my whole interest and good will of my Quarrell (*i.e.* quarry)."

"1766. Goldsm. Vic. W.I.V. Having given a hundred pounds for my predecessor's goodwill."

"1786. Lounger No. 79. On her marriage with the knight she had sold the good-will of her shop and warehouse."

"1836. Marryat Japhet VII, The shop, fixtures, stock-in-trade, and goodwill, were all the property of our ancient antagonist."

"1863. Fawcett Pol. Econ, IV. ii. (1876) 536. A solicitor can either sell the goodwill of his business, or leave it to his children."

USUAL FORM OF DEFINITION CRITICISED.—A usual form of definition of commercial goodwill, which, however, is now quite inadequate, is this—

"Goodwill.—The privilege, granted by the seller of a business to the purchaser, of trading as his recognised successor; the possession of a ready-formed 'connexion' of customers, considered as an element in the saleable value of a business, additional to the value of the plant, stock-in-trade, book-debts, etc."

This definition is too narrow in restricting the application of the term goodwill to an existing business or to a ready-formed "connexion" of customers, and, again, the recognised succession to a business or the possession of a ready-formed "connexion" of customers may be a privilege or the reverse, and so in this respect also the definition is unsatisfying.

In these days of joint stock enterprise very large sums are constantly paid to vendors of undertakings in embryo, over and above the value of any land, buildings, plant and stock which may be included in the bargain, for estimated further value which is represented by nothing except that which is in the nature of goodwill, and it is necessary to reconsider the whole subject and to investigate the bearing of modern developments upon it.

GOODWILL IS THE PRESENT VALUE OF FUTURE "SUPER-PROFITS."—It will be found that, except when arising out of personal considerations referred to below, there is never any real value existing in the form of goodwill unless an undertaking is reasonably expected to produce an extra-normal yield in the future, which may be called "super-profits," the term "super-profits" meaning the amount by which profits (that is, of course, true economic profits) exceed a normal rate of interest on capital invested. On the other hand, wherever there are expected future super-profits there is always real value existing in the form of goodwill. The term "real value" is used to distinguish it from imaginary value.

EXTENT OF THE SUBJECT OF GOODWILL.—Real value existing in the form of goodwill extends far beyond the limits which are generally assigned to it, and it is now generally admitted that its nature is common also to rights known under other names; thus real value existing under any of the following heads is in the nature of goodwill—

(a) Rights to carry on industrial and commercial enterprises, with the benefit of current contracts, including leases, and the use of trade-names, and trade-marks.

(b) Patent rights.

(c) Copyrights.

(d) Rights to exercise monopolies.

It should be noted that, except perhaps in the case of rights to exercise monopolies, all these

existing values are traceable to the exercise in the past of personal industry, skill and ability in creating enterprises out of which super-profits are expected to arise in the future.

Viewing the whole field of goodwill as it actually exists to-day, and bearing in mind that it is the present value of the right to receive expected future super-profits, it will be observed that goodwill arises not only out of the past work of the successful organiser of industrial and other profit-seeking undertakings to which the term is generally applied, but that it also arises out of the past work of those engaged in other and very different pursuits, though the values are then commonly known by other names. Thus, the past work of the inventor may have a present value which is described as the value of patent rights, and so also may the past work of the author, such value being known as copyrights. There is no economic difference between the nature of these several values, which have the common characteristic of arising out of the exercise in the past of personal industry, skill and ability. The legal protection from competition over considerable periods of years which, from ancient times, has been extended to the work of the inventor and to the work of the author is, however, a fact to be borne in mind in considering the degree of permanence likely to be enjoyed by these particular classes of values.

Rights to exercise monopolies include such statutory privileges as are possessed by municipalities to install and work tramways and other public services, and these rights are often sold for valuable consideration to joint stock companies formed for the purpose of exploiting them. This class of value is identical with goodwill, for it also arises solely out of the expectation of future super-profits.

Only Purchased Goodwill takes recorded and visible shape. While goodwill forms part of the present value of every profit-seeking undertaking expected to yield future super-profits, yet, as a rule, this value only takes recorded and visible shape and becomes a practical financial question if and when the goodwill of the undertaking has been purchased, that is to say, transferred from one person to another for valuable consideration. It is probable, therefore, that the bulk of the value really existing in the form of goodwill is not recorded in any financial books and accounts, and thus, as to the greater part of the subject, no question of its treatment in accounts ever arises. The reason is that in the majority of profit-seeking undertakings to which goodwill attaches, the valuable connection has been created and accumulated by ability and effort exercised whilst in the hands of the present owners. It is important to bear this in mind, for it will materially assist in arriving at a true

understanding of the nature of this value, which extends far beyond the limits of that comparatively small part recorded in financial books and accounts. In order to emphasise this important fact and to prevent confusion of thought, this part of the subject should be called "Purchased Goodwill," bearing in mind that the unqualified word "Goodwill" includes "Purchased Goodwill."

DEFINITION OF GOODWILL.—The following is suggested as a definition of Goodwill—

"Goodwill, in its commercial sense, is the present value of the right to receive expected future super-profits, the term "super-profits" meaning the amount by which revenue, increase, or advantage received, exceeds any and all economic expenditure incidental to its production."

Thus, subject to the qualification mentioned below, no present exchangeable value in the nature of goodwill can exist unless the expected future revenue, increase, or advantage either consists wholly of super-profits, or is greater than all economic expenditure incidental to its production. Such expenditure would include any and all current expenses, expired capital outlay (depreciation) on wasting assets other than goodwill, personal remuneration sufficient to secure continued successful management (which may possibly need ability of a high order), and a rate of interest on capital invested which will attract and retain any necessary capital, having regard to the degree of risk incidental to the character of the undertaking.

There is one necessary qualification to the above definition when it is applied to the goodwill of a professional practice, or of a business undertaking needing special knowledge, skill, and ability to carry it on successfully. In such cases it is often worth the while of the qualified practitioner, or of the trained man of business or trader, to pay a sum of money, by way of goodwill, although future super-profits are not expected to arise, in order that he may at once become possessed of an established connection, without which he would be unable to use his capabilities to the best advantage. The alternatives being for him either to attempt to build up a new connection, *ab initio*, or to accept service as a paid assistant to another, when, in either case, his earnings would be considerably less than he would expect if able at once to bring his special knowledge to bear upon an established connection. Thus, the value of the goodwill of an undertaking required for use in combination with the personal knowledge, skill, and ability of the purchaser may be due to, and will vary with, the degree of opportunity for profitable use which the prospective purchaser thinks he possesses.

Super-profits. Theory of Value. Having mentioned these special personal requirements as affecting the value of the goodwill of a certain

class of undertakings which, however, are perhaps of comparatively minor importance, it is necessary to consider and develop the theory of "super-profits," as being the foundation and real source of the value of goodwill. It has been pointed out that, apart from special personal requirements, the value of goodwill arises solely out of the inevitable and universal demand for super-profits, the meaning of which has been defined, and without the reasonable probability of super-profits, no real value in the form of goodwill can exist. The amount paid for purchased goodwill thus really represents a premium paid to secure an extra-profitable opening for the employment of capital.

Money can always obtain a Normal Annual Wage, without the Payment of an Initial Premium. It has been said that the term "super-profits" means the amount by which profits are expected to exceed a normal rate of interest on capital invested, and for the sake of illustration it may be assumed that the annual wage or hire (that is, interest) of money for secure and easily convertible investment averages 5 per cent., and, when subjected to the risks incidental to industrial enterprise, 7 per cent. These rates may be too high or too low, but that is immaterial for the purpose of illustration if it be granted that money demands at least some annual wage or hire increasing with the degree of risk incidental to its employment. Easily marketable gilt-edged securities now yield $4\frac{1}{2}$ per cent. per annum, which is a reason for, assuming $4\frac{1}{2}$ per cent. to be the minimum annual wage or hire of money.

There seems to be no doubt about the truth of the proposition that before it is possible to justify value being put upon the goodwill of any undertaking, it must be shown that the expected future annual profits exceed the normal annual wage or hire of the capital invested, having regard to the nature of the risk. This normal annual wage can obviously always be obtained by capital at any time without the payment of a premium, because there are always opportunities free of charge for the employment of capital at normal rates of interest. The payment of a sum for goodwill has the same effect as the payment of a premium and can only be justified if the opportunity offered for the employment of capital is of more than normal value.

The Vendor of Goodwill is entitled only to the Present Value of an Annuity equal to an Annual Share of Future Super-profits. In fixing the price to be paid for goodwill, the vendor cannot reasonably expect to secure for himself the equivalent of the whole of the future annual super-profits; he must leave a share of these sufficient to induce an alert purchaser to buy, and, for the sake of illustration, it may be assumed that, having regard to the vendor's secured position, he must

not expect to secure more than a one-half share. Then, again, the vendor is obviously only entitled to be paid the present value of an annuity equal to his share of each future year's super-profits, and even then his position will be infinitely superior to that of the purchaser, because he absolutely secures his share of these possible future profits by the receipt now of cash or its equivalent, whereas the purchaser is in the position of having already paid away a share of each future year's estimated super-profits, and, therefore, must make some annual provision to refund this share as a first charge upon the actual super-profits of each future year, before he can safely enjoy the remainder.

Super-profits can never exist permanently. With regard to the degree of permanence in value of purchased goodwill, it is important to observe that, owing to the operation of ever-present economic forces, super-profits themselves can never exist permanently, though they may sometimes continue to arise out of an undertaking for a great number of years. One principal reason for the temporary character of super-profits is the existence of competition. Commercial competition is universal and is constantly at work striving to secure a share in super-profits of all kinds wherever they appear, and whenever an undertaking is earning super-profits it will always tend to attract imitators. This operates to reduce, and will ultimately level, the earnings to a rate of profit equal to the normal rate of interest on the capital invested, having regard to the nature of the risk. Another reason why super-profits are always of a temporary character is that the demand for any commodity or service may at any time slacken or cease owing to all kinds of changing conditions, including new inventions. On accepted economic grounds, therefore, super-profits can never be treated as being in the nature of a perpetuity; they are essentially in the nature of an annuity extending over an unknown but limited term; and, therefore, the value of goodwill is not permanent.

Difference between the Present Value of an Annuity and the Sum of the Annual Payments. It is necessary now to consider the difference between the present value of the right to receive an annuity over a number of years and the sum of the future yearly amounts of that annuity. This difference in value is due to the fact that £100 due a year hence is worth less than £100 due now, for money can always earn a minimum annual wage of $\frac{1}{2}$ per cent., and, therefore, £100 due now will have increased to £104 a year hence. By the same process of reasoning, £96.154 due now will have increased to £100 a year hence, and the present value of £100 payable a year hence is £96.154, payable two years hence it is £92.456, and three years hence £88.9.

Thus, taking the value of money at 4 per cent. per annum, the present value of an annuity of £100 for three years is £277·51. This present value is built up by adding together a number of units, each of which units represents the present value of one future year's annuity as under—

INSTALMENTS OF ANNUITY					
	1st year.	2nd year.	3rd year.	Interest.	Total.
Present value of £100 annual instalments	96·15	92·46	88·90	—	£277·51
One year's interest at 4% for 1st year . .	3·85	3·69	3·56	11·10	—
	£100·	96·15	92·46	—	—
One year's interest at 4% for 2nd year . .	—	3·85	3·69	7·54	—
		£100·	96·15		
One year's interest at 4% for 3rd year . .	—		3·85	3·85	22·49
			£100·		£300·

The sum of the present value, amounting to £277·51, plus the sum of the interest from the present date, with yearly rests, to the date when each instalment of £100 becomes due, amounting to £22·49 equals £300, being the sum of the annual instalments. The present value of each succeeding unit in this sum is less than the one before, because the time to elapse before the year's annuity becomes due is one year longer in each case. This longer time obviously enables more and more compound interest to be earnable in the meantime on the money paid in advance, representing the present value of the succeeding units, thereby increasing that part of the effective consideration passing to the vendor in the shape of future interest earnable on the purchase money, and decreasing to a like amount that part payable to the vendor in cash now, which is called present value.

To put the matter in another form, the effective consideration which will have been received by the vendor of goodwill by the dates on which the purchaser expects to receive the super-profits he has bought is the present value plus something else. Take, as an example, the annuity of £100 for three years, the present value of which is, as stated above, £277·51. Suppose that this £277·51 is the amount paid to a vendor as the present value of goodwill, the expectation being that the purchaser is, in exchange, securing a benefit, the vendor's share of which will amount to £100 a year, and will extend over three years. The effective consideration passing to the vendor is £300, consisting of present value £277·51 plus interest at 4 per cent., amounting to £22·49, which he will be able to earn on the purchase money, from the date of purchase of goodwill to the time when each annual payment, representing his share, is receivable thus—

UNITS OF WHICH PRESENT VALUE IS COMPOSED				
	1st year.	2nd year.	3rd year.	Total.
Present value of good-will paid to the vendor	96·15	92·46	88·90	£277·51
Interest at 4%, which the vendor can earn on the amount of each unit between the present date and the date when each £100 which he sells is receivable	3·85	7·54	11·10	22·49
	£100·	£100·	£100·	£300·

This part of the subject is so important that a further illustration in tabular form may be useful. Taking the value of money at 4 per cent. per annum, the present value of the right to receive an annuity of £100 over a period of 100 years is £2,450·5, and the way in which this value is arrived at, by adding together a number of units, is shown in the table given below—

DECADES											SUMMARY		
Year of Decade.	1-10	11-20	21-30	31-40	41-50	51-60	61-70	71-80	81-90	91-100	Decades.	Present value of £100 annuity.	
1	96·154	64·958	43·883	29·646	20·028	13·530	9·140	6·175	4·172	2·818	1-10	811·090	33
2	92·456	62·460	42·196	28·506	19·257	13·010	8·789	5·937	4·011	2·710	11-20	547·943	28
3	88·900	60·057	40·573	27·409	18·517	12·509	8·451	5·709	3·857	2·606	21-30	370·172	15
4	85·480	57·748	39·012	26·355	17·805	12·028	8·126	5·490	3·709	2·505	31-40	250·075	10
5	82·193	55·526	37·512	25·342	17·120	11·566	7·8	5·278	3·566	2·409	41-50	168·940	8
6	79·031	53·391	36·069	24·367	16·461	11·124	7·513	5·075	3·429	2·316	51-60	114·131	7
7	75·992	51·337	34·682	23·430	15·828	10·693	7·224	4·880	3·297	2·227	61-70	77·103	6
8	73·069	49·363	33·348	22·529	15·219	10·282	6·946	4·692	3·170	2·142	71-80	52·086	5
9	70·259	47·464	32·065	21·662	14·634	9·886	6·679	4·512	3·048	2·059	81-90	35·190	4
10	67·556	45·639	30·832	20·829	14·071	9·506	6·422	4·338	2·931	1·980	91-100	23·772	3
	811·090	547·943	370·172	250·075	168·940	114·131	77·103	52·086	35·190	23·772		£ 2,450·502	100

Thus, the present value of an annuity of £100 is as under—

For ten years	:	£811.090	:	£811.090
For twenty years:	£811.090 +	£547.943	=	1359.033
For thirty years:	1359.033 +	370.172	=	1729.205
For forty years:	1729.205 +	250.075	=	1979.280
For fifty years:	1979.280 +	168.940	=	2148.220

It will be seen that no less than 88 per cent. of the present value of an annuity of £100 for one hundred years arises out of the payments to be received within the first fifty years of the period.

With the assistance of this table it is possible to realise more clearly the effect of the interest factor which is apt to be overlooked in considering the present value of goodwill. It has been said that the vendor of goodwill is selling nothing but the right to receive an expected future annuity. And, owing to the annual value of money or its equivalent, that particular future instalment of an annuity of £100 which is not due until the lapse of ten years is worth now £68 only; that one not due until the lapse of twenty years £46 only; that one not due until the lapse of thirty years £31, and so on. Looking at the other end of the table, it will be seen that the present value of that particular future instalment of an annuity of £100 which is not due until one hundred years hence is only £2; ninety years hence, £3; eighty years hence, £4; seventy years hence, £6; and sixty years hence, £10. Thus, assuming the price paid for goodwill to be no more than its present value, it is clear that substantially the whole of the benefit which has any considerable value is actually enjoyed by the purchaser within a period which cannot extend much beyond fifty years from the date of purchase, because that which is purchased is the right to receive an annuity over a number of years, and the annual payments of an annuity have comparatively little present value unless they are receivable within a period of fifty or sixty years. Even if an annuity continues during one hundred years, it will be seen from the table that 88 per cent. of the present value is attributable to the annual payments to be received during the first fifty years of the period.

SUMMARY OF CONCLUSIONS AS TO THE NATURE OF GOODWILL.—The above conclusions as to the nature of goodwill may be summarised thus—

(1) Goodwill is the present value of expected future super-profits, that is, the balance of profits remaining after providing for all incidental expenditure, including expired capital outlay on wasting assets other than goodwill, and personal remuneration for management, and after also appropriating a sum equal to a normal rate of interest on capital invested.

(2) The term "goodwill" includes not only the present value of rights to carry on industrial and commercial enterprises, but it also includes the present value of patent rights, copyrights, and rights to exercise monopolies.

(3) The bulk of the value actually existing in the form of goodwill is not recorded in any financial books and accounts. It is generally only that goodwill which has been purchased from a vendor which is so recorded, and which should, therefore, be called "purchased goodwill."

(4) The vendor of goodwill cannot reasonably expect to secure for himself the whole benefit of the future annual super-profits; he must divide them fairly with the purchaser.

(5) The vendor of goodwill is only entitled to be paid the present value of an annuity equal to his fair share of each future year's super-profits.

(6) Super-profits can never exist permanently, because commercial competition is universal and constantly at work, and also because the demand for any commodity or service may slacken or cease owing to changing conditions and new inventions, and, therefore, the annuity which the vendor of goodwill sells should never be treated as being in the nature of a perpetuity.

(7) Even if the annuity which the vendor of goodwill sells is treated as an annuity extending over one hundred years, it will be found that 88 per cent. of the present value arises out of the payments to be received within the first fifty years of the period.

Valuing the Goodwill of a Professional Practice.

It will be convenient to consider shortly how goodwill should be valued. Suppose the average profits of a professional practice after providing interest at 5 per cent. (an average rate) on capital, but before charging any sum for partners' services, are £6,000 per annum. There are two equal partners. One is to retire, selling his share of the goodwill to the remaining partner. First, it is necessary to deduct from the profits a sum to be agreed for the personal remuneration of the partners, say £1,200 each per annum. This will leave £3,600 "super-profits," of which the outgoing partner has been receiving one-half, or £1,800, but he cannot expect to retain the whole of this, and in view of his secured position, he may be satisfied if he gets the present value of one-half, equal to £900. The next point to consider is over how many years this annuity may reasonably be expected to continue as the result of the past work and influence of the retiring partner, and supposing ten years is agreed upon, it will be found on the above 4 per cent. table that, as the present value of an annuity of £100 for ten years is £811.09, therefore, $\times 9 = £7,300$, which, on the assumptions made, is the value of the goodwill, and proves to be rather less than two and a half years' purchase of the retiring

partner's former total annual income of £3,000 from the practice.

In valuing goodwill, it is necessary to endeavour to see into the future, and it is never possible to do this with very great success. In the case of established undertakings, it is customary, owing to this difficulty, to value the goodwill as being equal to some number of years' purchase of past annual so-called profits, often, however, omitting from consideration in computing those profits, such important factors of expense as expired capital outlay, personal remuneration for management, and a normal rate of interest on capital invested. In the case of new undertakings, formed to purchase and work rights of various descriptions, including patent rights, the wildest estimates of the value of these rights—that is, the goodwill—are often made, based on some rough-and-ready calculation prepared by the vendor, and put forward in a prospectus, which perhaps contains the names of well-known men who have, without sufficient thought, been induced to become directors. Owing to the difficulty of seeing forward in valuing goodwill, it has become customary to look backward and too readily to accept past events as an unerring guide to the future. But this cannot safely be done, and in seeking after better methods it is necessary to endeavour to isolate and separately examine, in the dim and uncertain light of future probability, each of the varying factors bearing upon the value of goodwill. Instead of looking too closely at past profits as a measure of the present value of goodwill, it will be well to consider the present value of a terminable annuity equal to that share of the expected future profits which may fairly be treated as belonging to the vendor as his reward for past work and the exercise of his knowledge, skill, and ability. The term of years over which such an annuity may be calculated to extend will vary with the circumstances of each case, but it will be found that, taking the value of money at 4 per cent. per annum, the distant instalments of an annuity have comparatively little value.

Testing the Reasonableness of the Purchase Consideration Paid for Patents, etc. The method of valuing goodwill which has been suggested above will be found useful to apply as a test of the reasonableness or otherwise of the very large sums constantly paid to vendors for various classes of rights, including patent rights. Thus, suppose the prospectus of a company is advertised offering 200,000 shares of £1 each for the purpose of acquiring and working a patented invention. Suppose the purchase consideration is £100,000, payable to the vendor in cash or shares at the option of the directors, so that out of the total issue there will remain £100,000 in cash available for the purchase of land, buildings, plant and

machinery, and for stock-in-trade, book-debts and working capital generally. It will be noticed that, although it is stipulated the purchase consideration may be paid to the vendor either in cash or shares, the shares are equivalent in value to cash, unless, indeed, public subscriptions are being invited to that which is worth less than the price asked. The vendor is selling an annuity equal to his share (say one-half) of the expected future super-profits, for which he is to receive as the present value £100,000. Suppose the price paid for the goodwill is considered as being the present value of an annuity extending over a period of twenty years, then by the aid of the 4 per cent. interest table set out above, it will be found that £1,359·033 being the present value of an annuity of £100 for twenty years, therefore, by a proportion sum, £100,000 is the present value of an annuity of £7,358. Twenty years is perhaps a reasonably long period to take as that over which substantial annual super-profits are likely to be earned. On this assumption, however, and supposing that, owing to his secured position, the vendor's share is, as stated above, only one-half of the expected future super-profits, then in order to justify the payment of £100,000 to the vendor as the value of the patent rights—that is, the goodwill—the average annual profits for the next twenty years should be expected to amount to £20,716, made up as under—

Expected average annual Profits.		
6% annual interest on £100,000, the capital invested (exclusive of the cost of goodwill)		£6,000
Balance being annual average super-profits.		
One-half sold and paid over to the vendor for goodwill	£7,358	
One-half retained by shareholders, who are thus induced to purchase the goodwill	7,358	
		14,716
		<u>£20,716</u>

Space will not allow of further illustrations and instances, but it will be found an interesting study to take the prospectus of any limited company offering shares for public subscription in which a value is put upon the goodwill, patent rights, etc., and examine and criticise this value by the detailed method suggested above. It will sometimes be found that what may before have looked a very attractive future financial prospect is considerably altered in appearance when viewed in the cold light of reason and of economic fact from which there is no escape

Nevertheless, it sometimes happens that the vendor's fair and proper share of the goodwill, either of an established undertaking or of a new undertaking, is equal to a large fortune; and no doubt shareholders in new undertakings formed to develop and work modern inventions sometimes make very large sums of money for themselves, as in the case of a limited company formed in recent years to develop a mechanical patent, with a capital of £48,000 which included working capital and also the amount paid to the vendor for the value of the patent, that is, for goodwill. The profit for the first year amounted to £149,000, or over 300 per cent.; and for the next year to £210,000, or nearly 450 per cent. But an undertaking such as this is not very often met with, and such instances are, unfortunately, more than offset by cases in which the profits from this class of enterprise are much less than expected.

Sale of Goodwill at Time of Profits' High-water Mark. It should always be remembered that in purchasing or sharing in the purchase of the goodwill of an undertaking, the purchasers are entering upon a speculation, and while, naturally, there are many exceptions, it is probable that in the majority of cases where the goodwill of an established enterprise is sold, the time selected by the vendor for selling is after several years of increasing prosperity. The profits may be near their high-water mark, and as by present custom the value of goodwill is computed as being equal to the sum of a given number of past years' profits, the value would in such cases be likely to be very much over-stated.

Writing off the Cost of Goodwill. It seems clear that wherever capital has been laid out in the purchase of rights to carry on industrial and commercial enterprises and remains as an asset in the books of an undertaking, some provision should be made and charged to Revenue Account in every year in which super-profits have been earned. This is the least that should be done, and, indeed, it is questionable whether it is sound financial policy to treat as a first charge upon the profits of each year, a sum equal to what has been called a normal rate of interest on the capital invested. Such a proposal, however, has the advantage of supplying a reason for allocating some part of the profits of each year first to the purpose of paying a dividend on the capital of the company. In some years the whole profits might not exceed, and might even be less than, the amount required for a dividend as measured by reference to the sum required for the payment of a normal rate of interest on the capital invested. This would not include the capital laid out in the purchase of goodwill, and in fixing a normal rate of interest regard should be had, in each case, to the nature of the incidental risk. Supposing this normal rate is agreed in a particular case to

be 6 per cent., and that the issued capital of the company is £120,000, of which £20,000 represents the cost of goodwill, the first charge upon the profits of each year will be 6 per cent. on £100,000 = £6,000, which is sufficient to pay a dividend of 5 per cent. on the whole issued capital of £120,000.

There is, perhaps, something to be said for contending that, when it is found in any year that no super-profits have been earned, nothing can be written off goodwill, because the super-profits purchased in the price paid for the goodwill having been proved not to exist in that particular year, cannot, of course, be refunded out of the profits of that year. This certainly seems to supply a measure of justification for permitting, as a prior charge, the payment of some dividend over the whole capital of the company out of the profits, before any provision is made towards writing off the cost of goodwill. It will no doubt be said that any attempt to put into operation a definite scheme of any such kind, would be impossible, and would, if adopted, often lead to the wrecking of a good undertaking in its early years; but the subject seems worth thinking out, and clear thinking may show that the good resulting from the adoption of some such method would very far outweigh any evil consequences.

The time is rapidly approaching when shareholders will expect directors of public companies in all cases to settle and adopt the use of a scheme or definite policy on reasonable lines for dealing with capital expenditure on goodwill. In the case of the company set out above, it is assumed that in return for the £100,000 paid to the vendor as the present value of the goodwill, the undertaking will be in the receipt of an annuity, coming to it in the form of annual super-profits, one moiety of which will amount to £7,358 for a period of twenty years. This term of years was taken for the sake of illustration and may, therefore, be assumed to be a reasonable forecast. If this is so, the company ought, without doubt, to settle and adopt the use of some scheme by means of which this £100,000 will be refunded out of the profits earned during the twenty years.

Supposing the expected future profits do, in fact, amount, on an average, to £20,716 per annum, the company will be receiving in this amount, the full annuity of £7,358, which, on the assumption made, was purchased from the vendor. It is not, however, necessary to set aside each year so large a sum as £7,358. On the other hand, it is desirable to provide a larger sum than £3,358, which is the amount necessary to be set aside each year and invested in a sinking fund in order to accumulate at 4 per cent. interest to a sum of £100,000 at the end of twenty years. The appropriate annual provision is something between the amount of the annuity which the company has purchased and the amount which would have

to be set aside for the purpose of a twenty years' sinking fund, and such a reasonable amount would be £5,000, or one-twentieth of £100,000.

Objections to the Sinking Fund Method. The principal objection to the sinking fund method is that there is no security whatever that its obligations will be carried out. It is apt to create a false sense of financial security. The efficiency of a sinking fund depends entirely upon the continuance and faithful performance of the duty of investing a fixed sum each year, and this duty is cast upon a necessarily changing management, over a long period of future years, during which unknown and unthought of economic changes and developments are likely to take place in the industrial world. Another objection is that the sinking fund method entails unnecessary and long continued risks to the money which must be invested in outside securities, always subject to fluctuations, however well selected and supervised, and whenever there is a failure to exercise sound and capable judgment, the risk of loss is greatly increased. The best use for capital gradually released by the operation of a scheme for refunding the cost of goodwill, would be to reduce the capital of the undertaking by gradual repayment, but in the existing state of the law this cannot at present conveniently be done.

It is quite true that if the plan suggested above for refunding the capital outlay of £100,000 on goodwill, in the case of the company mentioned, was adopted, and £5,000 of the capital was paid off every year over the period of twenty years, the company would in the twentieth year, assuming for the sake of argument that its annual profits did in fact amount to £20,716 per annum during the whole of the twenty years, find itself in the happy position of having a balance of £15,716 (being £20,716, less the £5,000 appropriated for goodwill) to distribute as dividend on the then reduced capital of £105,000, that is, £100,000 plus £5,000, the last annual appropriation for goodwill. From this it will be argued that in setting aside £5,000 each year out of revenue, too large a provision is made in the earlier years when the capital is larger, and too small a provision in the later years, when the capital is less. The same effect is produced, however, by the use of the sinking fund method, although this effect is then more obscure, for the true amount contributed each year to a sinking fund is equal to the amount of the annual instalment of the sinking fund plus the interest earned each year on the sinking fund investments, and in the case of a 4 per cent. sinking fund to accumulate to £100,000 at the end of twenty years, the first instalment amounts to £3,358 plus interest *nil*, and the last or twentieth instalment, amounts to £3,358 plus interest £3,717, equals £7,075, so that in the one case the annual provision is equal while the capital

grows less each year, and in the other case the capital remains equal while the true annual provision increases each year. The growing annual interest on a sinking fund is a product of the use of part of the capital, and it is a product which is commonly improperly omitted from record in the accounts of undertakings using the sinking fund method of accumulating funds.

The Vital Importance of the Subject Illustrated.

There are many cases of sound, prosperous and increasing businesses having among their assets items representing purchased goodwill. In each case the amount may look strictly reasonable, and it may be that the present profits are considerably larger, and seem likely to be more permanent, than when the goodwill was purchased. Under these circumstances, it is difficult to persuade the owners of a business that it is financially unsound to omit to make some regular provision, according to the nature of the case, for ultimately refunding the capital outlay on goodwill. But there seems no escape from the fact that it is unsound for the reasons already stated. That the subject is of vital importance to all who are in any way interested in the financial results of industrial and commercial enterprises, will be clear from a casual examination of company Balance Sheets, including some Balance Sheets, taken haphazard as a fair sample, from among a great many others—

(a) Provision Merchants. Capital, £350,000. Balance Sheet shows the goodwill, etc., £105,000, general reserve remains at £60,000.

(b) Coal Merchants. Capital, £900,000. Balance Sheet does not show position owing to goodwill being lumped with property, etc., for £700,000. Reserve account remains at £30,000.

(c) Brewery Company. Capital, £200,000. Balance Sheet does not show position owing to goodwill being lumped with premises and plant for £560,000. Reserve fund remains at £58,000, and Rebuilding reserve at £32,000. Reserve for purchase of debenture stock, £52,000, of which latter £6,500 is contributed out of the year's profits.

(d) Iron and Steel Company. Capital, £750,000. Balance Sheet does not show position owing to goodwill being lumped with land, buildings, machinery, plant, etc., for £840,000. There is no reserve fund.

(e) Fine Art Publishers. Capital, £500,000. Balance Sheet shows copyrights, patents and good will at £240,000. To general reserve fund £8,000, making it £48,000; to special dividend reserve £2,000, making it £40,000; and capital reserve remains at £9,000.

(f) Merchants and Shippers. Capital, £500,000. Balance Sheet shows goodwill £150,000. To reserve £10,000, making it £76,000; and to special reserve for ordinary dividends £10,000, making it £30,000.

Bearing in mind how largely the correct computation of annual profit or loss depends upon the sufficiency or otherwise of the amount of annual provision for expired capital outlay on wasting assets in conjunction with the fact that it is not customary to make any regular provision for expired capital outlay on goodwill, the importance of the subject becomes very apparent. Those desiring to make some regular annual provision, and who believe in the sinking fund method of accumulation, may be reminded that an annual instalment of £1 put by out of profits, and invested in outside securities yielding 4 per cent., will, at the end of forty-one years, amount to £100, and, therefore, an annual instalment of £100 so put by will in the same period of time amount to £10,000.

No Legal Obligation in English Law to Write off the Cost of Goodwill. There is at present no legal obligation in the English law to write off goodwill out of subsequently earned profits, and the whole of such profits may, from the legal point of view, be properly distributed as dividend. But this is no argument in support of the view that the neglect is not financially unsound. The gradual exhaustion of that part of the capital of an undertaking which is represented by the capital outlay on goodwill may be compared with the gradual exhaustion of capital represented by the capital outlay on the purchase of a colliery or other similar wasting property, the contents of which are gradually depleted in the process of earning the revenue of the undertaking. It may be recalled that—

"In *Lee v. Neuchatel Company* (41 Ch. Div. 1) it was held that if the objects of the Company include the sinking of capital in the acquisition of wasting property, even depreciation by waste is not necessarily a revenue charge, but may by the regulations be thrown upon capital. . . . If the Memorandum of Association provides that the object of the company shall be to sink its capital in a wasting property and acquire profit by working that property, then the gradual diminution of the property by waste is a gradual destruction of the company's capital, which may be within its objects legitimate . . . it is for the shareholders to say whether or not they will put by a sinking fund to meet the waste, and the proper place to find this is in the Articles. They may, if they like, but they are not bound so to provide."

PROVISIONS OF THE COMPANIES (CONSOLIDATION) ACT 1908 AS TO GOODWILL.—The following provisions of the Companies (Consolidation) Act, 1908, bear upon the question of goodwill and the disclosure of the cost and book value of this—

Section 26 provides for the filing with the

Registrar of Companies of an annual list of members and summary, and Subsection 3 states that

"The summary must also (except where the company is a private company), include a statement . . . in the form of a Balance Sheet audited by the company's auditors and containing a summary of its assets giving such particulars as will disclose the general nature of those . . . assets and how the values of the fixed assets have been arrived at."

And Section 81 provides that it must state

"(g) The amount (if any) paid or payable as purchase money in cash, shares or debentures for any such property as aforesaid, specifying the amount (if any) payable for goodwill."

MARKET QUOTATION OF SHARES AT A PREMIUM: ITS CAUSES AND MEANING DISCUSSED.

It has been stated above that the amount paid for purchased goodwill is a premium paid to secure an extra profitable investment, and when the shares in a joint stock company are quoted at a premium this premium, unless distorted and rendered artificial by bull and bear operations in the shares, represents the market's estimate of the value per share of undistributed profits already earned plus the present value per share of expected future super-profits, if any. In examining the published balance sheet of a joint stock company, with the object of ascertaining how far the premium at which the shares are quoted is due to the amount of undistributed profits already earned, and how much is attributable to goodwill (the present value of expected future super-profits), a number of difficult questions will be found to arise.

Assuming, for the sake of illustration, that the floating assets are all properly stated at their fair going-concern values in the balance sheet, and that the wasting assets are also properly stated at values arrived at after deducting from their cost all capital outlay expired to the date of the balance sheet according to the best available estimates, and assuming also that the liabilities are fully and properly stated on the other side of the balance sheet, then the amount (if any) by which the stated value of the assets exceeds the sum of the liabilities and share capital issued will represent the amount of the undistributed profits already earned. In such a case it is comparatively easy to compute the amount which is being paid for goodwill in the market price of the shares by deducting from the premium on each share, an amount equal to the undistributed profits apportionable to each share as shown in the balance sheet, the remainder of the premium being represented by nothing but the present value of expected future super-profits. In the case of a joint stock company with a capital divided into preference

the super-profits of this particular undertaking will continue over a period of twenty years, and that the 10s. attributable to goodwill in the premium at which the shares are quoted includes the present value of one moiety of the expected future super-profits, it will be found that, in order to justify the payment of 10s. per share for goodwill in the price paid for the shares, the average annual profits for the next twenty years should amount to £6,678. The reason is that 10s. per share is equivalent, on the total shares issued, to 10s. \times 50,000, or £25,000, and as £1,359 is the present value of an annuity of £100 for twenty years (see 4 per cent. table set out above), therefore, by proportion, £25,000 is the present value of an annuity of £1,839 for the same period, and the £6,678 is computed as under—

Expected average annual Profits.	
Normal 6% annual interest on £50,000, the capital of the company	£3,000
Balance being annual average super-profits.	
One-half paid for as to its present value in the quoted price of the shares	£1,839
One-half left for the benefit of the purchaser of the shares	1,839
	<u>3,678</u>
	<u>£6,678</u>

If the annual profits for the next twenty years are not expected to exceed £5,000 or £6,000, the price of £1 16s. 9d. for the £1 shares may be considered an excessive one. But the value of goodwill depends on future prospects rather than on past results, especially in the case of a young and vigorous undertaking.

The purchase of shares in a joint stock company at a sum which is greater than the nominal value plus the amount of the undistributed profits per share already earned, lays upon the prudent purchaser, who has bought his shares, not as a speculation but for investment purposes, the obligation to set aside out of each year's dividend a reasonable sum to repay to himself that part of the cost of the shares which is represented by nothing but goodwill, because the value of this goodwill is based upon future super-profits, which, as has already been pointed out, cannot be expected to continue permanently owing to the existence of commercial competition, as well as to changing conditions, new inventions, and the like.

In the case set out above, it is assumed that the super-profits will continue for a period of twenty years, and, for the sake of illustration, it may be

assumed further that the profits earned during that period enable a dividend to be paid which averages exactly 10 per cent. per annum; the purchaser will thus receive on his investment a dividend of 2s. per share each year, out of which, however, he should set aside 6d. per annum during each of the twenty years to repay to himself the 10s. represented by nothing but goodwill which was included in the premium he paid for the shares. It is assumed that, at the end of twenty years, the company is wound up and that the assets having been accurately valued throughout the period, the surplus after paying liabilities is sufficient to repay to the shareholders £1 per share, being the nominal value of the shares, and 6s. 9d., being the undistributed profit per share, which it is assumed has remained the same over the period of twenty years.

In considering the *pro formâ* balance sheet set out above, it has been assumed that the assets and liabilities are stated in the balance sheet at their full and fair going-concern values, but the determination of the values of assets at any given date is always a matter of estimate, with the exception of land (which, for accounting purposes, should be stated at cost, because the capital outlay thereon does not expire as it does in the case of wasting assets), easily marketable securities, and cash at bank and in hand, the values of which cannot be a matter of doubt. The values of other assets may be either over-stated or under-stated in a balance sheet. If they are under-stated, the effect is to create what is called a hidden reserve, and this condition may be within the knowledge of some operators in the shares, as a consequence of which the demand for the shares may cause the price to rise to a premium, which appears to those unacquainted with the facts to be excessive.

Suppose, on the other hand, that in the balance sheet set out above the values of the wasting assets, such as buildings, leaseholds, and plant and machinery are over-stated, owing to failure to deduct adequate provision for expired capital outlay (depreciation) to the extent of say £8,000, the effect is that one-half the reserve fund of £16,000, appearing in the Balance Sheet and purporting to be undistributed profits, is represented by nothing, because, owing to the Profit and Loss Accounts having been prepared in previous years without making adequate charges for expired capital outlay to the extent of £8,000, the profits of those years have been over-stated, and have been transferred in that over-stated condition to the reserve fund, which, if regarded as a surplus, is, therefore, over-stated to a like amount. Again, it is quite possible that the other assets appearing in the balance sheet, representing what is commonly called the floating capital, such as stock-in-trade and debtors, may be stated in the balance sheet at sums which may ultimately

prove to be excessive, and if this over estimate of value amounted to £8,000 or £9,000, it may be found that the whole of the supposed reserve fund is a myth. This subject is treated more fully in the article "Reserves and Reserve Funds," but sufficient has been said here to show the difficulty of judging the value of shares by reference to the balance sheet of an undertaking, and it will also be plain that the premium at which a share is quoted on the market cannot safely be considered to represent estimated goodwill only. The premium may be due to the accumulation of profits already earned but undistributed, and it may be due to nothing but market manipulation and rumours.

Effect of Issuing Shares at a Premium. In issuing shares at a premium to rank *pari passu* with shares of the same class already issued, the holders of those already issued shares are, to the extent that the premium is not represented by undistributed profits already earned, selling for a cash consideration part of their goodwill, and it is important to examine the bearing of this. Suppose a company with assets less liabilities fully and fairly stated representing a capital of £100,000 divided into 50,000 6 per cent. preference shares of £1 each and 50,000 ordinary shares of £1 each, and earning a regular profit of £10,500 per annum, which is distributed as follows—

Dividend on 50,000 6% Preference Shares	£3,000
Dividend on 50,000 Ordinary Shares at 15%	7,500
	<hr/> £10,500

Suppose the business can be profitably extended by employing more capital, and that 50,000 more ordinary shares of £1 are offered and subscribed at a premium of 10s. per share. This will bring in £75,000 in cash, of which £50,000 represents the nominal value of the new shares, and £25,000 represents the premium paid to the company (now including both old and new shareholders) in cash by the subscribers of the new shares.

The carrying out of this transaction indicates that the goodwill of the business (the present value of the expected future super-profits) is estimated to be worth £25,000. By doubling the number of ordinary shares the holders of the original shares have parted with their right to one moiety of the expected future super-profits attributable to the old capital in exchange for a one-half interest in the £25,000 premium received by the undertaking, plus the right to one moiety of the expected future super-profits attributable to the new capital. There is an important difference observable between the purchase in the market of shares at a premium, and the subscription for new shares offered at a premium.

In purchasing shares in the market at a premium, so far as this premium is attributable to goodwill, it should not extend to cover more than the vendor's (seller's) fair proportion of this goodwill, because the vendor here sells his whole interest to the purchaser of the shares and must be content to accept such a price as will leave some of the expected future super-profits to accrue to the purchaser of the shares as an inducement to buy, for the purchaser should certainly look for something more than a normal rate of interest on his money. But the issue of new shares at a premium is a transaction by which the old partners (old shareholders) admit new partners (new shareholders) to share with them the future super-profits of the undertaking, on terms under which the new partners purchase an interest in the old partners' rights to the existing goodwill, and thereafter the old and new partners will be commonly interested both in the amount of the premium and in the whole super-profits arising out of the capital contributed by both. This is a transaction which should be to the common advantage of each.

If at any time it happens that the £25,000 so received as a premium on the issue of the new ordinary shares, is not required for use as capital by the business, it may be distributed as dividends over the whole of the ordinary shares, either in one payment or in a number of payments spread over a series of years. The distribution of the premium in this way will, as regards the old shareholders, be merely paying to them £12,500 which the holders of the new shares have paid to the company on their account, in consideration of the old shareholders having given up their right to a moiety of the expected future super-profits. The old shareholders will get less of such super-profits in the form of future dividends to the extent of that which has a present value of £12,500, and as regards the holders of the new ordinary shares, they would, on a distribution of the premium, be repaid the £12,500 (one moiety of £25,000) which they advanced to the company in order to bring their new ordinary shares up to the value of the old ordinary shares, which, be it observed, will still be 10s. per share premium, attributable as to 5s. per share to the right to participate in the cash premium and as to 5s. per share for goodwill, because unless and until the new capital introduced into the undertaking commences to earn a super-profit, the value of the goodwill remains the same, for it is not increased by the mere issue of further capital. It is obvious that the £25,000 premium may properly be looked upon as a sum deposited with the company by shareholders which may be repaid to them without encroaching on or curtailing the share capital.

Assuming there are no undistributed profits

to complicate the question, the rule for ascertaining the value placed upon the goodwill of an undertaking which issues, at a premium, new shares tanking *pari passu* with shares already issued, is to multiply the number of those shares already issued by the amount of the premium per share at which the new shares are issued. The premium on the new shares is paid in order to bring them up to the computed value of the old shares, which value should remain the same after the issue of the new shares and the receipt of the premium, because, although the value of the old shares is decreased by the proportion of the goodwill formerly attaching to them which has been sold, the value is correspondingly increased by the share of the cash premium received which attaches to each old share. Thus, each share of the total shares issued has then the same value per share as had the smaller number of old shares, part of this value being now represented by goodwill, and part by the common right to the cash premium brought into the undertaking by the holders of the new shares.

Applicants for shares offered at a premium should consider the matter in this light, bearing in mind also that the so ascertained value of the goodwill attaching to the old capital investment in which they buy a share is the present value of the expected super-profits, and, therefore, is smaller than the sum of the annual super-profits from the old capital investment which should be received in future years. From the point of view of the old shareholders, the issue of new shares at a premium is a convenient way of cashing in advance estimates of future super-profits, or, to put the transaction in other words, cash received by a company as premium on a new issue of shares is an exchange for present cash or rights to expected future super-profits.

When additional shares are issued by a company at a premium supposed to represent the value of the existing goodwill, it is important, when considering whether or not the premium is a

reasonable one, to ascertain the amount at which the goodwill is valued on the premium basis. The table below shows the total computed value of goodwill involved when, say, £25,000 premium or 10s. per share is paid by subscribers on an issue of 50,000 new £1 shares, and how this varies with the proportion which the total of the new shares issued bears to the total of the old shares already issued and ranking *pari passu* with the new issue. The premium paid in cash goes into the business and does not go exclusively to the holders of the old shares, so that part of it accrues to the benefit of the holders of the new shares.

Thus, the value of each share in the new capital is equal to the value of each share in the old capital, the premium being now represented partly by goodwill and partly by the cash received as premium on the new issue of shares.

CONFIRMATION OF DOCTRINE HERE SET FORTH.—Remarkable confirmation of the doctrine set forth in this article is contained in an able paper on "Goodwill," by the late Mr. Francis More, C.A., Edinburgh, reprinted in the *Transactions of the Chartered Accountants Students' Society of Edinburgh*, Vol. XII, Session 1900-01. Dealing with the question "How the goodwill attaching to a trading concern may be valued as between a willing seller and a willing buyer?" Mr. More said—

"I will best explain my views as to how the goodwill of such concerns may be valued by supposing a case. Take, for example, a trading concern with tangible assets, the full going value of which is ascertained to be £100,000, and suppose it is earning, and is likely to earn, 8 per cent., or £8,000 a year, I would say that the total price should not exceed the value of the tangible assets, viz., £100,000, because no more than an ordinary return is being got. But suppose the concern is earning, and is likely to earn, 13 per cent., or £13,000 a year, then I think a fair price might be even annual payments of the extra £5,000, or

New Ordinary £1 Shares.	Old Ordinary £1 Shares.	Total new Capital.	Proportion of premium accruing to holders of New Shares.	Proportion of premium accruing to holders of Old Shares.	Proportion of Goodwill transferred to holders of New Shares.	Computed Value of Goodwill.	Premium per Share of Old Capital.	Premium per Share of New Capital.	
								Goodwill.	Cash.
50,000 50%	50,000 50%	£100,000 100%	£12,500	£12,500	50%	£25,000	10/-	5/-	5/-
50,000 25%	150,000 75%	200,000 100%	6,250	18,750	25%	75,000	10/-	7/6	2/6
50,000 10%	450,000 90%	500,000 100%	2,500	22,500	10%	225,000	10/-	9/-	1/-

a present payment of £26,030, being the amount of seven annual payments of £5,000, less 8 per cent. discount. In this case the price would be the above £100,000 plus £26,030, or together, £126,030. Suppose, again, it is earning 18 per cent., or £18,000 a year, then I think a fair price might be the above £126,030 plus five annual payments of £5,000, or a present payment of £19,963; in this case the price would be £145,993. Suppose, again, that the business is earning 23 per cent., or £23,000 a year, then I think a fair price would be the above £145,993 plus three annual payments of £5,000, or a present payment of £12,885; in this case the price would be £158,878. Of course, in every case the seller's statement of the profits earned would have to be carefully verified. I do not for a moment presume to say that the above "Table of Prices" ought to be adopted; the average ordinary trading return and the number of years' purchase of the marketable goodwill I have quoted, may be too high or too low; each buyer must judge for himself, after considering all the circumstances of the particular case he is dealing with. What I wish more particularly to say is, that, in my humble opinion, the plan of giving a present payment equal to so many years' purchase of the total profits is a haphazard plan, and that a buyer is much less likely to make a mistake if, before he fixes on the price he is prepared to offer, he first of all procures a careful valuation of the tangible assets, and then breaks up and values the marketable goodwill in some such way as I have indicated. I do not forget that in some cases it may be worth while to pay a small bonus for a ready-made business earning only ordinary trade profits; it is, however, only the excess profits which ought to be paid for under the name of goodwill. Some of you may be thinking that a concern with tangible assets worth £100,000, and earning £23,000 a year would be very cheap at £158,878, as the profits would yield a return on the price of about 14½ per cent. Before, however, forming your opinion I would ask you to wait till you have considered what I have to say under the next head of my paper."

And later in the paper, under the heading "What provision ought to be made out of revenue to replace the capital sum paid for goodwill?" Mr. More says—

"I will now venture to state my views as to what provision ought in prudence to be made to replace the price paid for goodwill, and this I will do in a single sentence. It appears to me that the period within which the price paid for goodwill should be replaced out of revenue, ought, to a large extent at least, to be regulated by the number of years' purchase of the profits which the price represents. For instance, in the case which I have assumed in order to illustrate my

views as to how the price should be ascertained, I assume that £26,030 would be a suitable present payment to make for a goodwill which produced £5,000 a year in excess of the ordinary return. This present payment of £26,030 represents seven yearly payments of £5,000 (less discount at 8 per cent.), and I am disposed to think that, in such a case, one-seventh of the present payment of £26,030 should be set aside yearly out of revenue until a reserve of £26,030 was reared up. If this plan were adopted, the result would be, so far as the payment of dividends is concerned, that the ordinary shareholders would only get during the first seven years 8 per cent. on their money, plus any increase on the profits beyond the amount dealt with in fixing the price, and plus also any saving which might be effected by raising money either on debenture or on preference stock at a lower rate than 8 per cent. Of course, the profits might fall below the amount reckoned on when the purchase was made, and in that case the shareholders would have to judge whether they would continue to set aside yearly the amount I have indicated, and be satisfied with smaller dividends. The shrinkage of the profits would, however, only emphasise the risk which had been run in purchasing the goodwill." (See also ACCOUNTS, CRITICISM OF, p. 18; AUDITING, p. 91; BALANCE SHEET, p. 150; LIQUIDATORS, ACCOUNTS OF, p. 650; PARTNERSHIP ACCOUNTS, p. 745.)

GRANT COETORUM.

This term applies where a grant of probate or letters of administration is made in the first instance for a portion of the estate, and a subsequent grant is made for the residue. (See also EXECUTORSHIP ACCOUNTS.)

GRAPHICAL REPRESENTATION OF STATISTICS.

(See STATISTICS.)

GROSS PROFITS.

The difference between the cost price and the selling price of goods after taking into consideration the stocks at the commencement or end of the period. In the case of manufacturing, the cost price of material, together with the wages and other charges necessarily incurred in producing the goods, represents their cost. (See also ACCOUNTS, CRITICISM OF.)

GROUND RENT.

A landowner who has land conveniently situated for building purposes, having resolved to develop an estate by the erection of buildings upon it, frequently lets out the same to a builder under a building lease (*q.v.*). The lease is generally for an extended period, say, ninety-nine years, and the rent reserved is of a trivial amount. This

is the ground rent. The builder agrees with the landowner to erect a certain class of house or houses within the fixed period, and very frequently it is arranged between the parties that instead of a lease being granted to the builder an agreement to build shall alone be stipulated for between the landowner and the builder, and the former agrees to grant a lease to the nominee of the builder when the building is completed. This is generally the purchaser of the building, and the new owner and his successors become liable for the ground rent during the existence of the term. There are then two rents, if the building is let to another person, the rent of the building and the ground rent. At the close of the stipulated period the ground and the building upon it revert to the landowner. By statute, 4 Geo. II, c. 28, a ground landlord is empowered to distrain on the premises for the ground rent which is due and not paid. It is this right, especially, which makes ground rents such delectable and secure investments.

Ground rents payable, being taxed before payment, are not allowed as deductions from profits assessable to income tax. It is, therefore, advisable to record them in a separate Ground Rents Payable Account, instead of including them under the old-fashioned heading of rents, rates and taxes. They are subsequently transferred to the debit of Profit and Loss Account, where they form a separate and distinct charge, which is readily available for writing back when the assessment to income tax is being computed.

In checking this charge, the auditor should have reference to the leases, in order to ascertain what amount of ground rents are payable and when they fall due. Ground rents are not payable in advance. There is consequently a danger of the accruing portions, especially in the case of new rents, being overlooked. The auditor should see that proper apportionments of the accruing liability are included in the Balance Sheet; and that rents receivable under sub-leases are properly brought into account.

In the case of there being numerous ground rents receivable, a rental showing the amounts of the rents, the due dates, the sums received and the outstanding arrears should be brought into use. It will be the duty of the auditor to see that all ground rents receivable are included in the rental, by reference to counterpart leases; that all new rents created from time to time are added; that the rents received are properly accounted for and credited to Profit and Loss Account, and that there is no undue accumulation of arrears.

GROUPING OF ITEMS.

(See AUDITING, p. 82.)

GROWING CROPS.

For the purpose of their inclusion in the book-keeping records, growing crops must be valued.

The method of valuation depends upon the nature of the crop, but it is usual to take acreage as the basis. The estimated value of the crop is debited to the Crop Account, and credited to Profit and Loss Account. Subsequently the Crop Account is credited with the sum realised by the disposal of the asset. The items so credited will include cash received from sales of produce, produce used for seeding, produce used for pig and poultry food, etc. The balance on the account, which will thus be ascertained in the ensuing period of trading, should be transferred direct to the Capital Account, this account being credited if the realisation exceeds the valuation, and debited if the reverse is the case. The reason that this surplus or deficiency is not carried to Profit and Loss Account is that it is desirable to keep the records of each crop separate.

It is customary to value the crop at a figure approximating its marketable value. It is, therefore, necessary that an estimate of the probable cost of marketing the crop, which will include expenditure upon wages, threshing, carting, etc., should be reserved for. The estimated value of the crop thus appears in the balance sheet as an asset, and the estimated expense of harvesting and marketing it as a liability.

The auditor should direct his attention to satisfying himself that the valuation is made on a conservative basis, and that the cost of reaping the crop and placing it upon the market is fully provided for in the accounts.

GUARANTEE.

This is a contract whereby one person, who is called indifferently the guarantor or the surety, undertakes to be answerable to another person for any loss in respect of a debt, default, or act of a third party. Before there can be any question of guarantee, there must be a legally binding contract existing between two parties other than the guarantor or surety, and the guarantor is only called upon to fulfil his part in the transaction if the obligation between the others has not been carried out. This statement must be taken subject to an exception when the principal debtor is an infant. Suppose that an infant enters into a contract for goods other than necessaries. This, of course, is not a contract binding upon the infant; but if a surety guarantees the payment, he will be held responsible, because he would either be estopped from setting up the contractual incapacity of the infant principal, or he would himself be treated as the principal.

As a guarantee is a contract, the ordinary rules of offer and acceptance apply, and therefore the guarantee must be given by the guarantor to the principal creditor and accepted by him, and not to the debtor, for it is to the former that the guarantor binds himself.

Since a guarantee is an undertaking to be answerable for the "debt, default, or miscarriage" of another, the contract must be evidenced by writing, and the note or memorandum which is required in order to comply with the fourth section of the Statute of Frauds (*q.v.*) must be forthcoming when any action is brought. The note or memorandum must contain the names of the parties and the particulars of the transaction. But, by reason of the Mercantile Law Amendment Act, 1856, it is not necessary that the consideration should be set out, although there must be a consideration, unless the contract of guarantee is under seal. The note or memorandum must be stamped with a sixpenny stamp. A deed would naturally need a 10s. stamp.

It is not always easy to distinguish a guarantee from an indemnity, and nice points often arise as to whether a guarantee refers to one particular transaction or to a series of transactions, in which latter case it is called a "continuing guarantee." Everything turns upon the special circumstances of the case, and the authorities are too voluminous for citation.

A guarantor is only bound under his contract if the principal debtor fails to perform his obligation, and the extent of his liability will be measured by the contract itself. Also the guarantor will be released if there is anything in the shape of fraud or misrepresentation, as well as if the parties to the original contract act in such a manner as to vary the nature and the extent of the liability undertaken by him in the first instance. There must be no secret or collusive arrangements between the creditor and his debtor, which might affect the guarantor in any adverse manner.

If a guarantor is called upon to pay under his guarantee, he is entitled to certain rights, although their value may not be particularly great. These rights are—

(1) Against the principal debtor. He can recover all moneys properly paid under the guarantee, together with interest upon the same, or, if no moneys have been paid, he can take proceedings to compel the principal debtor to exonerate him from liability.

(2) Against the principal creditor. In return for discharging the debt under the guarantee, the surety has a right to be placed in the same position towards the principal debtor as the creditor is. All securities and other rights, such as judgments, must be transferred to him.

(3) Against co-sureties. When the contract of guarantee is entered into by several sureties, any one of the latter, on paying the amount fixed by the guarantee, can claim contribution from his co-sureties. And the right of contribution is not affected by the fact that the sureties are bound by different instruments. If, however, the various sureties are bound in varying amounts, they must

contribute proportionally to the amount guaranteed, and not equally. In reckoning the sureties, when there are several, only those are counted who are able to pay. Thus, if there are three co-sureties, and one of them has become insolvent, the surety who has had to pay the debt can compel the remaining solvent surety to pay one-half of the sum guaranteed, if he has had to pay the whole, and not one-third only.

GUARANTEE, CONTINUING.

(See CONTINUING GUARANTEE.)

GUARANTEE BOND.

A bond given by a guarantor or surety, under which the guarantor or surety holds himself responsible for the performance of certain specified duties by the person for whose fidelity he vouches. A bond of this kind is frequently given when the person whose fidelity is vouched for occupies a position of great responsibility or trust.

GUARD BOOK.

A book in which documents are pasted for safe protection and numbered consecutively, the book being used for invoices, receipts, or transfers of shares. Its great advantage is that the documents cannot readily be removed, and that immediate reference is afforded to the particulars as given on the document itself. Against these the disadvantages are that the book is somewhat cumbrous, and, owing to the bulk of the documents, dust is easily admitted inside the book.

In the case of an Invoice Guard Book, in order to compress them into as small a space as possible, the invoices are often folded, the number, date, name of the firm from whom the goods were purchased, and the amount, being written outside. The amount is also extended into the cash column which is provided for the purpose in the Guard Book. The unfolding and refolding of invoices is, however, a very troublesome matter, and a better plan is to fold the invoices as little as necessary, leaving the name on the invoice heading showing, and to paste the invoices at the bottom instead of at the top edge, extending the amount opposite each name.

The Ledger posting folio is sometimes placed on the invoice and sometimes in a folio column provided in the book.

The use of Guard Books is gradually being discontinued, owing to the advent of better filing systems, the Purchases Journal taking their place for invoices, and share transfers often being filed in a loose-leaf binding.

GUERNSEY, APPOINTMENT OF AUDITOR TO COMPANIES REGISTERED IN.

(See AUDITING, p. 62.)

HABENDUM OF A DEED.

THAT part of an indenture (*q.v.*) expressed in the words "to have." The full expression is generally "to have and to hold," which is often spoken of in its entirety as the "habendum," but in reality the words "to hold" are the "tenendum." The full phrase "to have and to hold" is, as a general rule, introductory to the declaration of the "uses," to, for, or upon which an estate is granted, and the office of the phrase is only to limit the certainty of the estate granted; therefore "no person can take an immediate estate by the habendum of a deed when he is not named in the premises; for it is in the premises of a deed that the thing is really granted."

HEAD OFFICE CHARGES.

The allocation of Head Office Charges against the individual branches must necessarily depend on the circumstances of each case. The method of apportionment is always a difficulty. It may be proportionate to the turnover of each branch, or may be a fixed sum; or a fixed percentage of the total head office charges may be debited to the branch. These bases are, however, usually so unsatisfactory that it is a common practice to credit the trading profits of the branches to a General Profit and Loss Account, and to debit the whole of the head office charges to this account.

In checking the head office charges, the auditor should examine the expenditure with a view of proving that no expenses which ought to be charged directly against any branches are included in the account, and, where there is a fixed basis of apportionment of the charges, he should see that each branch is duly debited with its proper share of the expenses, calculated in accordance with the method adopted. (See also BRANCH ACCOUNTS.)

HEALTH AND UNEMPLOYMENT INSURANCE DEDUCTIONS.

The Health Insurance Acts and the Unemployment Insurance Acts require that contributions to these schemes shall be made by the State, the employer, and the employee. As regards the two last named, the contributions at present required in respect of each insured person are as follows—

HEALTH INSURANCE		TOTAL	
Employer 5d.	Employee, if a Woman, 4d.	.	9d.
Employer 5d.	Employee, if a Man, 5d.	.	10d.

UNEMPLOYMENT INSURANCE

Employer 10d.	Employee, if a Man of 18 or over, 9d.	1s 7d.
" 8d.	" " Woman of 18 or over, 7d.	1s 3d.
" 5d.	" " Boy of 16 and under 18, 4½d.	9½d.
" 4½d.	" " Girl of 16 and under 18, 4d.	8½d.

The employer is liable in the first instance to pay the contributions of both himself and the employee, and this he does by means of stamps which he fixes to the insurance cards, subsequently deducting from the wages of the employees the amount payable by each. In the books of account the matter may be dealt with in either of the following ways—

(1) The Wages Account may be debited with the gross amount of wages, that is, the amount before the employees' contributions are deducted, and the employer's contribution can be debited to State Insurance Account. This method is frequently used in places where the insurance stamps are purchased weekly as required.

(2) In the case of firms which buy large quantities of stamps at a time the cost of these is debited to State Insurance Account. The *actual* wages paid are debited to Wages Account, and a transfer is periodically made from the State Insurance Account to the debit of the wages account of the amount represented by the employee's contribution. The Wages Account is thus brought up to the gross amount, and the balance of the State Insurance Account shows the amount payable by the employer.

HEATING APPARATUS.

The cost of installing a heating apparatus may be added to capital, provided a fairly heavy rate of depreciation is charged against revenue in respect of the loss in value due to wear and tear and obsolescence.

The auditor should verify the cost of the apparatus by reference to the original contract and the engineers' certificates of amounts due to contractors, together with the contractors' receipts, for sums paid to them.

HEREDITAMENTS.

The general name for freehold lands or houses, though in reality its meaning is extended to those things which pass to the heir upon an intestacy. The full phrase, "lands, tenements, and hereditaments," goes to express the whole of the real property of a person.

HIDDEN RESERVES.

(See SECRET RESERVES.)

HINDE PALMER'S ACT.

Until the year 1870 it was always a hardship in the administration of the estate of a deceased person that those creditors whose debts were by specialty, that is, created by deed, were preferred in the order of administration to those who claimed under simple contract. It will be obvious that in the case of an insufficiency of assets to satisfy all claims the specialty creditors might easily be paid in full and the simple contract creditors left entirely out in the cold. It was to prevent this inequitable condition of affairs that the Act known as Hinde Palmer's Act was passed in 1869, and became operative on the 1st January, 1870. No preference is now given to one class of creditors over another, and if the estate is not perfectly solvent there is a rateable reduction made all round. The Act has no application where a creditor has a lien, charge, or any other kind of security for the payment of his debt. It should also be noticed that an executor is allowed to retain his own simple contract debt so as to defeat specialty creditors. *Re Harris*, 1914, 137 L.T. 182. (See RETAINER.) If there is a right of retainer the assets of the deceased's estate must first be applied rateably between the creditors by specialty and by simple contract, then the claims of the specialty creditors must be satisfied to the extent of the amount allotted to them, and it is out of the residue, namely, that to which the simple contract creditors are entitled, that the executor must first deduct any debt that is due to himself.

HIRE-PURCHASE.

Hire-purchase is the usual term employed to denote all those transactions in which the payment takes the form of equal periodical instalments over a given period, and in which the legal property in the goods does not vest in the hire purchaser, tenant, or lessee, until the agreed terms and conditions, which are commonly embodied in an agreement, have been fulfilled. Until such consummation, the legal property vests in the lessor. Simple hire (*i.e.* without the concomitant of purchase) explains itself. The following cardinal points in hire-purchase transactions may, therefore, be stated—

1. Goods under hire-purchase do not vest in the tenant until the completion of the obligations of the agreement.
2. The consideration or price may be divided into three portions, cost, cost of credit, and profit, which together equal the selling price.

There are various modes of recording such

transactions. Take, for example, the following instance.

Purchase consideration £2,000, payable in ten years by equal annual instalments, including interest at the rate of 5 per cent. per annum.

The annual instalment is 259·00931, which is

the solution of $\frac{2000}{An}$, An being the usual symbol

for the present value of £1 per annum, and may be expressed numerically in its application to our transaction as—

$$1 - \frac{1}{(1.05)^{10}} \div .05$$

Instalments in hire-purchase transactions, however, are in practice payable over a shorter period, in monthly, quarterly, or half-yearly sums, and if that in our illustration were payable, say half-yearly, we should merely convert the formula just stated into—

$$\frac{2000}{\left(1 - \frac{1}{(1.05)^{10 \times 2}}\right) \div .025}$$

Analysing the transaction over the entire term of the agreement, we have—

Years.	Annual Instalment.		DISSECTION.			
			Capital.		Interest.	
	£	s. d.	£	s. d.	£	s. d.
1	259	0 2	159	0 2	100	0 0
2	259	0 2	166	19 3	92	0 11
3	259	0 2	175	6 2	83	14 0
4	259	0 2	184	1 5	74	18 9
5	259	0 2	193	5 6	65	14 8
6	259	0 2	202	18 10	56	1 4
7	259	0 2	213	1 9	45	18 5
8	259	0 2	223	14 10	35	5 4
9	259	0 2	234	18 7	24	1 7
10	259	0 2	246	13 6	12	6 8
TOTAL	2,590	1 8	2,000	0 0	590	1 8

Look at the mode of record from the manufacturer's and tenant's points of view.

As regards the manufacturer or lessor, the stock or other account may be credited with the gross at cost, and a Hire-Purchase Account debited.

The tenant's account will be debited with the periodical instalment as it becomes due, and Hire Purchase Account, Interest, and Profit and Loss Accounts credited with their due proportions thereof. The balance of the Impersonal Hire-Purchase Account, when written up, will show

from time to time the outstanding cost of the goods under hire-purchase agreements.

As regards the tenant, he will credit the seller with each instalment as it becomes due and debit interest and payments on Hire-Purchase Account with their respective proportions thereof, and when the transaction has been completed he will transfer the balance of the Hire-Purchase Account to the proper account concerned. The following may be taken as a mode, among others, of apportioning the profit and the amount of cost contained in each instalment devised and applied to certain cases by the writer.

Time.	Rental.	COMPOSITION OF RENTAL.		
		Proportion of Cost in each Instalment.	Proportion of Profit in each Instalment.	Proportion of Cost of Credit in each instalment.
(1)	(2)	(3)	(4)	(5)
	£ s. d.	£ s. d.	£ s. d.	£ s. d.
1	259 0 2	127 4 1	31 16 1	100 0 0
2	259 0 2	133 11 5	33 7 10	92 0 11
3	259 0 2	140 4 11	35 1 3	83 14 0
4	259 0 2	147 5 2	36 16 3	74 18 9
5	259 0 2	154 12 5	38 13 1	65 14 8
6	259 0 2	162 7 1	40 11 9	56 1 4
7	259 0 2	170 9 5	42 12 4	45 18 5
8	259 0 2	178 19 10	44 15 0	35 5 4
9	259 0 2	187 18 10	46 19 9	24 1 7
10	259 0 2	197 6 10	49 6 8	12 6 8
TOTAL	2,590 1 8	1,600 0 0	400 0 0	590 1 8

With regard to the figures in column (3)—

The instalment is . . .	£ 259 0 2
Less interest . . .	100 0 0
	£159 0 2 and
$\frac{£159 \text{ 0s. 2d.} \times 1600}{2000} = £127 \text{ 4s. 1d.}$	

To arrive at the amount in the same column in subsequent years, simply add 5 per cent. to those in previous years.

For the sums in column (4) we simply take 25 per cent. of the sums in column (3).

It is very desirable that a table, such as that sketched above, be prepared for every transaction, covering its entire tenure, with additional columns for, say, date of debit, folio, amount debited, and date received as a subsidiary record.

Such a course is particularly essential in cases where the terms, amounts and periods are of a miscellaneous nature.

In the system of accounting in practice, provision should be made for the proper treatment of returns, which require careful consideration. In the wagon hire-purchase trade we may encounter an intermediary—a wagon finance company, whose object is obvious (*i.e.* the purchasing of

wagons, locomotives, trolley stock of every kind, and letting the same on hire, upon terms which will provide for the wagons becoming the property of the hirer at the expiration of agreed periods). Some of the companies do not engage in manufacturing business.

Until recently considerable doubt has prevailed in regard to the incidence of Income Tax in relation to hire-purchase transactions. In the wagon hire-purchase trade, the Inland Revenue Authority seems to have acted principally and generally on their own view that such instalments were substantially part of the capital purchase, and that they were, consequently, capital payments. This view, however, was not upheld in a case (1913) decided in the Scottish Law Courts, and the following extracts from instructions issued to the surveyors of taxes serve to indicate the change of attitude that has taken place following the decision to which we allude—

“The lessee of wagons under a hire-purchase agreement shall furnish to the surveyor of taxes a copy of the agreement together with a certificate from the wagon builder, or other satisfactory evidence as to the price at which the wagons would have been sold for cash at the date of the agreement hereinafter referred to as the initial value. The difference between the initial value and the aggregate amount payable under the agreement shall be treated as hire and allowed in equal annual amounts spread over the terms of the agreement.

“Depreciation shall also be allowed on the initial value from the beginning of the agreement in accordance with the provisions of the Income Tax Acts, at a rate to be settled by agreement between the lessee and the Crown, or by appeal to the Income Tax Commissioners.”

With regard to audit, in addition to the duties pertaining to the usual audit of accounts, the auditor will *inter alia* deal with the following matters.

He should carefully examine the agreements, as recorded in the Agreement Register, in the form that we have partially indicated, with the actual documents, check the debits to the personal Hire-Purchase Accounts therefrom, see that all irrecoverable debts have been properly dealt with, and, as far as possible, that adequate provision has been made in respect of all outstanding debit balances of a doubtful character. He should also see that the composition of such debts for the period under review has been properly analysed, that the proper proportions have been credited to the Hire-Purchase and other respective Accounts, and that no credit has been taken for prospective profit, but only for profit on the instalments debited, subject, of course, to any necessary reservation. Moreover, he will see that the exact procedure in force for dealing with returns is adequate and

equitable, involving as it does the question of liberal provision for depreciation.

HIRE PURCHASE ACCOUNTS.

In the consideration of the methods in which Hire Purchase Accounts should be dealt with in the books of the manufacturer or seller and in the books of the purchaser, the effect of the agreement setting out the contract must, of necessity be closely examined.

What has become commonly known as a hire purchase agreement is one providing for payment of an article or articles by instalments, and such agreement may provide either that the goods are purchased outright or that the purchase may be completed only if the hirer so elects, and if he does not so elect the instalments are then in the nature of payment for hire only.

The essential difference between agreements of this nature is that in the one case, on default in payment of any instalment, the balance of the amount named in the agreement may become immediately payable and can be sued for, whereas in the other case on default in payment of any instalment the seller has the right to call for the return of his goods, and can sue only for those instalments which are in arrear.

It will, therefore, be appreciated that in order properly to set out the transactions in the accounts so that the real position may be recorded in accordance with the spirit of the agreement, it is necessary to examine the agreement and to ascertain its effect.

The transaction must therefore be regarded from two points of view, that is to say, from the point of view of the seller, or manufacturer, and from the point of view of the person who takes the goods on hire purchase.

SELLER'S BOOKS.—Regarding the transaction from the point of view of the seller where the agreement amounts to a sale, that is to say, where he is in a position to sue for the balance of the purchase money unpaid on default being made in payment of any instalment, it will manifestly be incorrect to credit the total amount to be received to the Sales Account, debiting a similar amount to the customer, for two reasons, viz.—

(1) Part of the amount to be received is in the nature of interest which has been added to the cost price of the goods and should, therefore, not be credited to Sales Account;

(2) Such interest has not yet been earned.

In order properly to record such a transaction in the seller's books, the amount named in the agreement must be divided into two parts, viz.—

(a) The amount representing the cost price of the goods;

(b) The interest which has been added.

The figure of interest must itself be divided in

order to ascertain the proportionate part charged in each instalment.

Where the amount representing the interest has been calculated on a fixed percentage basis, this is, of course, simple, since the question will resolve itself into a calculation of the interest charged at such known rate on the reducing figures of principal.

In some transactions, however, a lump sum is added to the cost price representing interest, and is not calculated on a definite rate of interest.

Where this is so, a mathematical calculation is necessary to arrive at the amount of interest charged in each instalment.

Having ascertained such amounts, the procedure is as follows—

The purchaser is debited with the cost price of the goods forming the subject-matter of the agreement, Sales Account being credited. As each instalment falls due the purchaser is debited, and Interest Account is credited with the ascertained amount of interest which is the proper charge on the principal which has been outstanding since the date of the previous instalment. It is convenient to head the account for each purchaser with a memorandum stating the essential parts of the agreement and with a table showing the amount of interest included in each instalment. An alternative method is to insert on the debit side of the customer's account the entries for interest which will require to be made but leaving the folio column blank. As each instalment falls due, the double entry is completed by crediting the appropriate amount of interest to the Interest Account, at the same time filling in the posting folio in the folio column against the item of which the posting is completed.

PURCHASER'S BOOKS.—In the books of the purchaser, the transaction will be put through in a similar, but converse manner, the Asset Account being debited with the amount of the cash price of the goods, the seller being credited. The necessary interest entries will be put through in a similar manner to that explained above, but, of course, conversely also.

It will be seen that, in either of the above cases, by crediting the hirer with the instalments in the books of the seller or by debiting the seller in the books of the hirer (as the case may be) on the completion of the last payment the account will be balanced.

DEPRECIATION.—It must be borne in mind that depreciation must be charged in the books of the purchaser to provide for the wasting of the asset from the date when the article is purchased, in the same way as in the case of an article purchased in the ordinary way for one payment down (see elsewhere).

CONTINGENT SALE.—Where the Hire Purchase agreement provides that on failure to pay

any instalment the seller has the right to call for the return of the goods and to regard the instalments paid as in the nature of hire payments only, the question is naturally more difficult to record in the books of either party since not only does the matter of interest come into consideration, but the question is further complicated by reason of the fact that until the purchase is completed by payment of all the instalments provided for (and usually a further nominal payment) it is impossible to decide whether such instalments are in the nature of hire only or whether they include a proportionate part which should be properly regarded as a "Capital" payment.

In such a case the "Suspense" system is the one which should be adopted in the books of the dealer.

SELLER'S BOOKS.—In this system the interest included in each instalment is ascertained in the manner already described.

The accounts with the customers are kept in a "memorandum" Hire Purchase Ledger, each account, besides being headed with the name of the customer, bearing a note of the transaction, the terms of the agreement, and a table of the interest included in each instalment calculated as though the transaction were a sale.

To the debit of each account are inserted the instalments to be paid and the due dates of payment.

A separate "Hire Purchase Account Receipts Book" is kept, ruled as given below—

In this subsidiary Cash Book are entered all receipts on account of Hire Purchase Agreements, the daily total only being entered in the General Cash Book. The items in the "Cash Received" column are posted to the Memorandum Ledger, the folio being inserted in the column provided for that purpose. Each item is analysed, as shown, into the columns provided for "Principal" and "Interest," the amounts being ascertained by

reference to the information shown at the head of the Memorandum Ledger accounts.

At the end of each week, month, or quarter, whichever is the most convenient, the subsidiary Cash Book is totalled and posted as follows—

1. The total of the "Principal" column is posted to the credit of a "Hire Purchase Receipts Suspense Account" in the Impersonal Ledger.

2. The total of the "Interest" column is posted to the credit of Interest Account in the Impersonal Ledger.

As each transaction becomes completed a Journal entry is put through as follows—

(a) If all instalments are paid in due course, "Hire Purchase Receipts Suspense Account" is debited and "Sales Account" is credited with the cash price of the goods.

(b) If default is made and possession is regained of the goods, "Hire Purchase Receipts Suspense Account" is debited and "Hiring Account" is credited with the total of the "Principal" amounts contained in the instalments paid, the memorandum account being noted, in the latter case, that the transaction is closed.

It will be appreciated that, in this system, interest is credited as it is earned and received, and, on the other hand, no credit is taken for a sale until it is an accepted fact, and should the payments turn out to be in the nature of hire, credit is taken to a "Hiring Account" only when it has been definitely ascertained that they should be so treated.

On drafting a Balance Sheet at any time, the cost of the goods out on Hire Purchase Account is included in the item of stock appearing in the Trading Account and appears as an asset in the Balance Sheet, the balance of the "Hire Purchase Receipts Suspense Account" appearing on the left-hand side of the Balance Sheet.

The balances on the Memorandum Ledger will naturally not be brought into the Balance Sheet

FORM I.

Date.	Particulars.	Folio.	Cash Received.	Principal.	Interest.	Daily Cash Total.	Cash Book Folio.

as debtors, which is in accordance with the spirit of the agreement, nor will credit be taken for any profit on sales nor for hiring until such revenue is actually ascertained by the termination of the various transactions.

It may be argued, as an objection to this system, that, whether the transaction be a "sale" or a "hire," some profit has been made and should be taken credit for during the time in which the transaction has been running and that the taking of such profit to credit should not be delayed until the completion of the transaction.

This objection cannot be regarded as a very serious one. In the case of the first year of the existence of a concern whose chief business it is to sell goods on the Hire Purchase System, there will be a certain hardship since but few transactions are likely to be completed before the first year's accounts are drawn, but in after years the matter will adjust itself.

It will be readily appreciated that in the case of an agreement with the effect which is explained above, the "Suspense" system is the only one which can be logically adopted and put into effect without bringing confusion into the accounts.

The receipts of instalments, except for the ascertained interest, are borne on the "Suspense Account" until the proper destination of the receipts is found, which can only be on the completion of the transaction, either by payment of all the instalments, or by the operation of the default clause and the return of the goods.

The balance on the Suspense Account ascertained at any time will be, therefore, composed of sales and hire receipts, and as soon as it is possible, they are transferred away to the proper account.

The Memorandum Ledger serves the purpose also of a useful register of stock out on hire purchase, and each account should be headed with a summary of the goods and the cost price.

On the stocktaking date all that is necessary is to extract a list of such cost prices noted on the accounts which have not been closed by payment of all instalments or by the operation of the default clause and the return of the goods as explained previously.

PURCHASER'S BOOKS.—In dealing with the matter in the purchaser's books the effect of the agreement has to be considered in a similar manner.

In the case where, at the option of the purchaser or on default being made, it is provided in the agreement that the goods shall be returned and the amounts paid are to be regarded as hiring payments, as already pointed out, it is impossible to state whether the payments involve treatment as a purchase or as a hiring expense until the transaction has been completed.

In the purchaser's books, therefore, the system explained as the one to be adopted in the seller's

books should be applied, the entries being put through in a converse manner.

The cash price is ascertained as before, and also the amount of interest charged.

A Memorandum Account is opened for the purpose of keeping the account with the seller, and this account is credited with the various instalments. At the head of this account, for the purpose of reference, the details of the transaction are set out and a table of the principal and interest items included in each instalment.

When payment of an instalment is made it is entered in the Cash Book on the credit side in two amounts, one representing the principal payment, and the other the interest payment, treating the transaction as in the nature of a purchase for this purpose.

The total of the two amounts, *i.e.* the amount of the instalment, is entered on the Memorandum Account on the debit side.

The "principal" amount is debited from the Cash Book to a "Hire Purchase Suspense Account" and the "Interest" amount is debited to the Interest Account.

On the termination of the transaction the matter is dealt with as follows—

(1) If all instalments have been paid, Hire Purchase Suspense Account is credited with the cash price and the asset account is debited.

(2) If the transaction has been closed by operation of the default clause and return of the goods, or at the option of the hirer, Hire Purchase Suspense Account is credited and Hiring Account is debited with the total of the "principal" amounts included in the sums paid as instalments.

In the former case the Memorandum Account will automatically close and be ruled off, and in the latter case the account will be noted as closed.

On drafting a Balance Sheet, the balance of the Hire Purchase Suspense Account will be shown on the right-hand side.

It may be argued that, should a transaction turn out to be a hire, the debits which have periodically been made to Interest Account are incorrect since they are themselves part of the hiring payment. It should be remembered, however, that, in addition to the hire payment which includes the dealer's profit and provides for his loss in depreciation of the goods, he is entitled to interest on the capital sunk in the goods out on hire, and for that reason the debit to Interest Account in the hirer's or purchaser's books is a correct one, whichever way the transaction may turn out.

Instances where Hire Purchase Accounts form a very important part of a business are in the accounts of furnishing concerns, piano dealers, and similar traders dealing in goods which represent a considerable outlay on the part of the

purchaser, and where terms allowing the purchase price to spread over a number of months or years are largely taken advantage of. The importance of an adequate system allowing proper results to be ascertained cannot, therefore, be underestimated, and unless such a system is in operation, fictitious figures of profit will be arrived at and serious fluctuations occur in various years where sales are taken credit for before they are accomplished facts and instalments are not analysed into their proper component parts.

In the theatrical, music hall, hotel, and cinematograph businesses, advantage is often taken of the Hire Purchase System, and the accounts can be seriously affected by improper treatment of the payments made under this heading.

In the books of a concern where such transactions are the exception, the rough and ready method is often adopted of debiting the instalments as they are paid to a Suspense Account.

If a Balance Sheet be drawn before the transaction has been completed, the total of the instalments paid is brought into the right-hand side of the Balance Sheet as "Instalments paid under Hire Purchase Account."

If the transaction be closed before the drawing of the Balance Sheet, a transfer is made from the Suspense Account to the debit of the Asset Account of the figure of the cash price and to the debit of the Interest Account of the figure of interest charged if the completion of the transaction is effected by payment of all the instalments. If the transaction be closed by the return of the goods the figure standing to the debit of the Suspense Account is transformed to Hire Account.

Although this method is an incorrect one, since the charge for interest or hire may not be spread over the proper period in which the benefit has been received, yet, in the case of an isolated transaction, no very serious objection can be taken if the amount involved is not considerable.

It will readily be understood that where transactions of this nature involve a considerable amount, the proper method, as explained above, must be adopted, and more particularly is this so in the case of an undertaking such as a colliery, where wagons are purchased on the Hire Purchase System.

WAGONS HIRE PURCHASE AGREEMENT.—

An agreement for the hire purchase of wagons has the effect that the manufacturer gives immediate possession of the wagons for the use of the colliery on the understanding that if the hirer makes the prescribed number of payments, the ownership of the wagons shall pass to him on the payment of a further nominal sum. Agreements vary in nature, but the effect as far as the accounts are concerned is as above. On default in payment of the prescribed instalments, the manufacturer

has the right to regain possession of the wagons and to treat the sums paid as hire payments only.

It will be appreciated that in such a case large sums may be involved which, if incorrectly treated in the books of either party to the transaction, will seriously affect the accounts.

Whatever the concern may be, however, the treatment of the payments should be the same except, perhaps, in the case of an isolated transaction involving an inconsiderable sum.

The question of the proper treatment of Hire Purchase Accounts is one which has given rise to a great amount of discussion on account of the fact that in some quarters it has been held that, from the dealer's point of view, the transaction should be treated as a sale at the cash price immediately the transaction has been entered into, interest being debited periodically. Undoubtedly, this view is an incorrect one, since profit is taken immediately, although not earned, and amounts appear under the heading of "Debtors" in the Balance Sheet, although such amounts are not payable at the date of the balance and, under the terms of the agreement, *may never become payable*.

The system described above avoids such an inaccuracy in treatment. The only objection, from the point of view of the dealer is that, in the system described, no profit is taken until the transaction is terminated in one of the two ways contemplated by the agreement.

This objection is not an important one in the case of a concern carrying through many transactions in the course of a year, particularly where the payment is not spread over a large number of years, and the majority of Hire Purchase transactions come under this heading.

Where, however, each transaction involves a large sum of money, and consequently has an important effect on the Trading Account of any one year, the position is somewhat different.

In such a case each system has its drawbacks, because a large profit will be taken either at the commencement or end of the transaction, according to which system is adopted.

SYSTEM PROVIDING FOR TAKING A PROPORTION OF PROFIT IN EACH YEAR.—The ideal system, of course, is one which will provide for the taking of a proportion of profit in each year in which the transaction is running and yet, in whichever way the transaction terminates, will not have taken profit for a larger sum than can be anticipated if the transaction is completed in the way least favourable to the dealer.

Such a system is the following, which can be claimed as the ideal one for a dealer to adopt and is an extension of the system already explained in the case of the dealer's books. It has, necessarily, an element of complication in it and requires

As already explained, stock will not include the cost of goods which form the subject-matter of

completed transactions, since the sale is completed and ownership of the goods transferred to the purchaser.

Should the transaction, by operation of the default clause or by return of goods, turn out to be a hire, the following Journal entry will be put through—

Hire Purchase Receipts Suspense Account.

Dr. to

Hire Account (or Trading A/c.).

Being the difference between the "principal" sums included in the instalments paid and the profits already transferred.

It will be seen that it is not necessary to put through the entries as each transaction terminates and that the whole of the adjustments may be left until the date arrives for the drawing of the accounts.

On a careful examination of each Memorandum Account a schedule may be extracted containing the material for all the necessary entries to be made at the end of each financial year. Form II shows the rulings and headings which will be convenient.

The total of column 3 will be the figure of stock to be included under that heading in the Balance Sheet or to be carried to the General Stock List.

The total of column 4 will be debited to Hire Purchase Receipts Suspense Account and credited to Trading Account.

The total of column 5 will be dealt with in the same way as column 4.

The total of column 6 will be debited to Hire Purchase Receipts Suspense Account and credited to Hire Account (or direct to Trading Account).

The above system is the only one which may be regarded as correct in its treatment of the question, and it is one which may be put into operation without much more clerical work than is required in the system previously explained.

Provided that the Memorandum Ledger containing the accounts of the customers is carefully and accurately kept, and that the details of each transaction are detailed in convenient form at the head of each account, it is only on the occasion of the drawing of the periodical accounts that extra time is involved in extracting the details for the necessary Journal entries. Such extra time is amply repaid by the resultant accounts, which set out the exact position and the profit earned in each period as nearly as it is possible to do so and in accordance with the effect of the agreement entered into. (See also AUDITING, p. 95; BALANCE SHEET, p. 153.)

HOLDER IN DUE COURSE.

This is the title given to the person who has, legally, the paramount claim upon a bill of exchange. He is, of course, the person who has the possession of the bill, and by the Bills of

Exchange Act, 1882, he is the one who has taken it *bonâ fide* and for value, the bill itself being regular and complete on the face of it, and without any notice of any kind of defect whatever in its history. The holder in due course is entitled to demand payment from the acceptor upon the maturity of the bill, and the mere production of the document is *primâ facie* a complete statement of his claim. If the acceptor does not pay, he can then sue him by action at law or he can give notice of his claim to any other person who is a party to the bill and, if payment is refused, sue him in the same way as he could sue the acceptor. There is only one way in which a holder in due course can be defeated, and that is when the bill happens to bear a forged or an unauthorised signature. He can never claim *through* a forged signature, nor can he sue *through* an unauthorised signature, unless the party whose signature it purports to be has ratified the same. But a forged or an unauthorised signature does not bar the holder's remedy at law against any indorser who has signed subsequently to the making of the forged or unauthorised signature. The position of a holder in due course is so important that two sections of the Bills of Exchange Act, 1882, namely, 29 and 30, are exclusively devoted to a statement of his position and rights. These sections should be most carefully studied and remembered. (See also BILL OF EXCHANGE.)

HOLDING COMPANY.

A holding company is one which is formed for the purpose of consolidating, co-operating, preserving, and developing the interests; promoting economy and efficient organisation in operation; and harmonising (in some cases) the work of certain other companies, each of which pursues its own particular avocations while retaining its existence as a separate corporate entity, the holding company not being a working or operating undertaking.

The directorate of the holding company is composed of certain of the directors of the subsidiaries concerned therein.

The shareholders, in what ultimately become the subsidiaries of the holding company, exchange their holdings therein for equivalent interests in the holding company, which thus obtains ownership of the entities which are parties to the controlling scheme, and incidentally indirectly become owners of controlling interests in further companies whose capital and other issues are owned by the subsidiaries themselves.

HOLDING OUT.

Although it is not easy to define the term with exactitude, its meaning is not difficult to understand. It refers in general to the action or actions of any person who behaves in such a manner as

to lead others to believe that he occupies a position to which he is not rightfully entitled. It is, in fact, a species of deceit. When a person thus acts, or holds himself out, as occupying a certain position, he may render himself liable for all the consequences which would naturally follow if he did in fact actually occupy that position. The term is most frequently met with in cases of partnership. A man may not be a partner in a firm, and yet he may so interfere with the business of the firm that third persons are fully justified in believing that he is, in fact, one of the partners. It would, then, be inequitable that he should escape all liability, when he has, probably, by his conduct, induced the outside world to place special faith in the strength and stability of the firm with which he has pretended to be associated. The Partnership Act, 1890, has provided for the case of "holding out" by section 14, which runs as follows—

"(1) Every one who by words spoken or written, or by conduct represents himself, or who knowingly suffers himself to be represented, as a partner in a particular firm, is liable as a partner to any one who has on the faith of any such representation given credit to the firm, whether the representation has or has not been made or communicated to the person so giving credit by or with the knowledge of the apparent partner making the representation or suffering it to be made.

"(2) Provided that where, after a partner's death, the partnership business is continued in the old firm's name, the continued use of that name or of the deceased partner's name as part thereof shall not of itself make his executors or administrators, estate or effects, liable for any partnership debts contracted after his death."

HORSEKEEP AND STABLE EXPENSES.

Horse-keep and stable expenses, including the wages of employees engaged upon work in and about the stables, form a charge against Profit and Loss Account. In order to maintain the equity of the charge the account should be charged with the stock of provender on hand at the opening of the period, and credited with that on hand at the close of the period. In cases in which the whole or a portion of the provender is the produce of land in the occupation of the firm or company owning the horses, a transfer should be made, charging the Horse-keep Account with the value of the provender supplied.

The auditor may be able to test the accuracy of this account by calculating the cost per horse, either per week or over the period. Usually this cost, after taking into account any qualifying items

such as the rise or fall in the price of provender, increased wages, etc., will be found to work out at a fairly constant rate. Any exceptional increase or decrease should be the subject of a close inquiry.

HORSES, CARTS, ETC.

It is advisable that separate accounts should be kept for (1) horses, and (2) carts and other rolling stock, in order to facilitate a proper valuation of these assets from time to time.

Where a large number of horses are kept the original cost of the animals should be charged to Horses Account and depreciation at the rate of (say) 15 per cent. written off for a period of five years, after which the balance may remain as a permanent asset, provided that the number and quality of the horses is maintained and that all new purchases are debited to revenue.

Where there is a small number of horses, all new purchases should be charged to Horses Account, and 20 per cent. to 25 per cent. per annum written off as depreciation. The actual rate will, of course, depend upon the nature of the work done by the horses. At frequent periods there should be a re-valuation of the horses, and the Ledger balance adjusted to this figure, and the future rate of depreciation determined by the experience.

The auditor should require the production of a properly certified valuation in this case, and should, from time to time, satisfy himself that the number of horses has been maintained and that none have been illicitly disposed of, by insisting on the production of a schedule of the animals. It should be remembered that these animals may easily be disposed of for cash.

Carts, lorries, and other rolling stock will be subject to a depreciation dependent upon the use to which they are put. Generally speaking, 15 per cent. to 20 per cent. per annum should be written off, all repairs being charged to revenue.

HOSPITAL ACCOUNTS, AUDITORS AND.

(See AUDITING, p. 117.)

HOTCHPOT.

Where an intestate dies and leaves personal property, the same is divided according to the provisions of the Statute of Distributions (*q.v.*). If, however, any considerable sum of money has been advanced to one of the children—supposing that the division has to be made between children—by the testator during his lifetime, this sum must be brought into account before the division is made. This is called "bringing into hotchpot." It only occurs as between the children of male intestates. Thus, a widow takes her share of the estate as it stands at the time of death; she has

nothing to do with hotchpot. And if a woman dies intestate, the question of hotchpot never arises, whatever advances she may have made. (See also EXECUTORS AND ADMINISTRATORS; EXECUTORSHIP ACCOUNTS, p. 466.)

HOTEL ACCOUNTS.

(See TABULAR LEDGER.)

HOUSE DUTY.

(See INHABITED HOUSE DUTY.)

HOUSEHOLD EFFECTS.

A comprehensive term covering all the furniture of a household and all fixtures which have not, by their nature, become a part of the freehold.

HOUSEKEEPING EXPENSES.

Household expenses do not, of course, form any part of the trading charges of a business, and their inclusion in business accounts should be discouraged. When, however, they are included in the book-keeping records, they should be posted direct to a Household Expenses Account, whence they should be transferred periodically to the proprietor's Drawings Account. They

must not be charged against Profit and Loss Account.

The auditor should carefully examine the invoices with the object of assuring himself that no household expenses are wrongly included amongst the ordinary trading charges. Where goods for private and business purposes are purchased in bulk, he must be satisfied that a proper proportion is charged to household expenses. The same applies to rents, rates and other expenses which are incurred in respect of both business and private purposes. The Household Expenses Account should be submitted for examination in detail to the proprietor and be approved by him, to ensure that the account has not been misused to hide improper payments.

In some businesses it is the custom to arrange the remuneration of certain officials and servants to include the rent, rates and taxes of their dwelling-houses, and the coal, gas and water consumed by them. Household expenses of this nature form a proper charge against trading and should be debited to Wages Account, or Salaries Account, as the case may be. In such circumstances the auditor should refer to the service agreements, to ascertain that none but the charges provided for therein are being paid.

ILLEGAL CONTRACTS.

THESE are contracts which are of no legal validity, because they are either unlawful in any of their terms, or because they contemplate the prosecution of anything which is unlawful in its results. All agreements to commit a crime or a civil wrong are absolutely void. So are those which are opposed to what is called "public policy," that is, those which contemplate the carrying into effect of anything which is calculated to be detrimental to the general interest of the community. In addition to these, certain agreements have been made invalid by various Acts of Parliament, and the number of such statutes is constantly increasing. A distinction must be made, however, between certain contracts which are not made specifically void but are unenforceable by action. Of this last-mentioned class reference need only be made to gaming and wagering contracts. Gaming is not illegal, but any agreements arising out of it are unenforceable by process of law.

IMMEDIATE PARTIES.

In the case of bills of exchange, the parties to the instruments are the drawer, the drawee (who, on acceptance, becomes the acceptor), the payee (who may or may not be the same person as the drawer), and the indorser. There may, of course, be numerous indorsers. Any two of the parties who are immediately connected with each other as to liability upon the instrument are known as "immediate parties." Thus, the drawer and the acceptor, the acceptor and the payee, the payee and the indorser who indorses immediately after the payee, if the bill is payable "to order" and therefore needs the payee's indorsement, and any indorser and the person who indorses immediately before or immediately after him are immediate parties. All other parties to the bill are called "remote parties."

IMMOVABLE PROPERTY.

According to English law, property is generally divided into real and personal. But for some purposes, especially connected with questions of International Law, another division is made, namely, into movable and immovable property. Immovable property consists of tangible things which cannot be moved, through being connected with the soil. It comprises land and houses or buildings, whatever the interest may be which a person has in the same. It will be seen, therefore, that the term does not coincide with our

"real property," for what are called "chattels real" are included, that is, such interests as leaseholds, which are, according to English law, personal property. The distinction becomes of importance when a person who is domiciled in this country and who possesses immovable property in some other country dies or becomes bankrupt; for it is a principle of the English courts that they will not entertain any suit which is concerned with immovable property abroad, seeing that, in time of peace, it could have no effective machinery for rendering a judgment of any real value.

IMPERSONAL ACCOUNTS.

These comprise the Nominal Accounts, such as purchases, sales, wages, rent, insurance, carriage, travelling expenses, general expenses, discounts, interest, etc.; the Real Accounts, such as land and buildings, machinery and plant, fittings and fixtures, stock and goodwill; and also any other accounts which are not those of persons, as Bills Receivable, Bills Payable, Reserves, etc.; and the Profit and Loss Account.

IMPERSONAL ITEMS.

(See BALANCE SHEET, p. 141.)

IMPERSONAL LEDGER CONTROL ACCOUNT.

(See SELF-BALANCING LEDGERS p. 855.)

IMPLIED CONTRACT.

Where parties place themselves in such a position and act in such a manner that the law will infer that there is an agreement in existence between them, the contract is said to be an "implied contract," in contradistinction to an "express contract," in which all the terms are clearly set out. According to Blackstone, an implied contract is one "which reason and justice dictate, and which the law, therefore, presumes that every man undertakes to perform." The only difference between an express and an implied contract is in the mode of proof, the former being proved by direct evidence, the latter by circumstantial evidence. The commonest example is where A runs a public vehicle and B enters the same without saying a word. The law implies a contract between the parties, that A will carry B and that B will pay A a reasonable price for the same.

IMPLIED TRUSTS.

All trusts which are recognised in equity are divided into two main classes, those which are

set out in express terms by the parties creating the trusts, and those which are not so set out but which are to be inferred from the unexpressed but presumed intention of the parties. These latter are known as implied trusts. They are to be distinguished from constructive trusts in which no question of intention, either express or implied is considered, but in which the court raises, or constructs, trusts for its own purposes simply.

IMPOSSIBLE CONSIDERATION.

Consideration is at the base of all simple contracts, and provided that there is a consideration, the law will not, generally speaking, inquire into its adequacy, unless fraud is alleged. Nor will it trouble about the nature of it, unless the consideration is, in fact, impossible, when the contract will be rendered void for want of consideration. There are three kinds of impossibility—

1. **ABSOLUTE IMPOSSIBILITY.**—This is the case of an agreement to perform anything which is impossible by the laws of nature, as, for example, to alter the velocity of light or sound, or to pierce a hole through the earth.

2. **LEGAL IMPOSSIBILITY.**—This is the case where an act is positively forbidden by the law of the land.

3. **ACTUAL IMPOSSIBILITY.**—This third kind of impossibility is the most important of all, and arises when parties have contracted with respect to a state of affairs which they have assumed to exist, but which has actually been changed between the time of the formation of the contract and the due date of its performance without the knowledge of either. In this third case, however, it must be borne in mind that the parties may, by the terms of the contract, so bind themselves that the impossibility will have no effect upon the legal liability, and the contract itself remain good.

IMPRESSED STAMPS.

These are special stamps which are required to be used for the following documents—

Assignments of Policies of Life Insurance.
Conveyances.

Inland Bills of Exchange (except when the bills are payable on demand, at sight, on presentation, or at a period not exceeding three days after date or sight, when either an adhesive or an impressed stamp may be used).

Inland Promissory Notes; Letters of Allotment; Memorandum of Deposit; Mortgages; Scrip Certificates; Transfers.

Stamps may be impressed on all instruments or documents except where an adhesive appropriated stamp is necessary. (See APPROPRIATED STAMPS.). In certain cases, *e.g.* agreement under hand, either an impressed or an adhesive stamp may be utilised.

IMPREST SYSTEM.

A system of keeping Petty Cash under which a cheque is drawn for such an amount as is estimated will cover the Petty Cash expenses for a certain period, say a week, a fortnight, or a month, the amount being credited to the bank and posted to a Petty Cash Account in the Ledger. The cheque is given to the petty cashier, whose balance in hand at any time, plus the amount he has expended since the last balancing, should equal the amount of the cheque, which is known as the Imprest amount.

When the period has expired, the petty cashier analyses the Petty Cash Book and submits it to the cashier, together with vouchers for payments, and the cashier, after examination, initials the Petty Cash Book and hands the petty cashier a cheque for the amount expended, so placing him again in possession of the original amount.

The cashier enters the analysed details and the total in the Cash Book, posting direct to the Nominal Ledger Accounts, the Petty Cash Account remaining unaffected.

In a business where the amount of Petty Cash expenditure fluctuates considerably, instead of balancing periodically, this may be done whenever the petty cashier is getting short of cash, this in no way affecting the principle of the Imprest System.

If desired, the Petty Cash in hand may be cleared at the end of each year by crediting the cash instead of the bank with the last amount expended, and also with the balance, debiting the bank with the balance (which is paid in), and debiting cash and crediting the Petty Cash Account with the total. (See also PETTY CASH.)

IMPROVEMENTS TO PREMISES, ALTERATIONS AND.

(See ALTERATIONS AND IMPROVEMENTS TO PREMISES.)

INCHOATE INSTRUMENT.

This is the name given to any instrument which is incomplete in form. Many examples of such an instrument may be given: a stamped bill form simply signed by a person, and handed by him to another person to fill up and complete as a bill; a form in which the date of payment is not inserted; a bill in which the amount is not stated; a form of cheque containing the drawer's signature and nothing else. The danger which attends the circulation of such instruments is obvious, and the Bills of Exchange Act, 1882, has endeavoured, by Section 20 of that statute, to lessen the same by enacting as follows—

“(1) Where a simple signature on a blank stamped paper is delivered by the signer in order that it may be converted into a bill, it operates as a *prima facie* authority to fill it up as a complete bill for any amount the stamp will cover, using the signature for that of the drawer,

INCOME TAX.

(See APPENDIX, p. 945.)

INCORPOREAL CHATTELS.

The interests or rights of a personal character which have no physical existence. The best examples of these are patents, trade marks, and copyrights.

**INCREASE OF CAPITAL :
LIMITED COMPANIES.**

(See LIMITED COMPANY ACCOUNTS, p. 636.)

INDENTURE.

An indenture is a deed under seal between two or more persons, and the name is derived from two Latin words *in*, and *dens*, a tooth. In former times a deed was written in two parts on one parchment, and then a division was made by dividing it with an indented or wavy line passing through a word, generally *chirographum*, which was written between the two parts of the deed. Each of the two parties to the deed received a part, and when at any time the two parts were brought together again, it showed that they were the correct documents when the indents agreed and the divided word was made whole. In point of fact, the indenture corresponded to the old tallies. All this is now of historical interest only, as, by an Act passed in 1845, it was enacted that "a deed executed after the 1st October, 1845, purporting to be an indenture, shall have the effect of an indenture although not actually indented." The date of an indenture is at the commencement of the deed, and the document invariably commences as follows: "This Indenture, made the first day of June, 19.., between John Jones of, etc., of the first part and James Smith of, etc., of the second part, etc." (See DEED POLL.)

INDIRECT CHARGES.

(See COST ACCOUNTS, p. 348.)

INDORSEMENT.

This word is used in two senses. In the first it signifies the act of writing on the back of any document, and in the second it means the matter which is there written. By writing his name upon the back of any document, the person who does so identifies himself with it in some manner or other. But the most common way in which indorsements become of importance is when the documents dealt with are negotiable instruments or instruments indicating the title of some person or persons to certain things named therein. By indorsing, for instance, a bill of exchange or promissory note, the indorser makes himself a party to the same, and incurs certain liabilities, unless the bill or note is an accommodation one, by the mere fact of indorsement coupled with delivery, whether he receives any consideration

for the same or not. Again, the holder of a bill of lading, which is not a negotiable instrument but a document of title, by indorsing the same and delivering it to another person indicates *prima facie* that he has passed the property and all right in the goods named in the bill to the transferee which he, the indorser, possessed.

It has been held that the writing upon the face of a document may have the same effect as an indorsement, in the same way that an acceptance of a bill of exchange may be good although written upon the back of the bill. It is, however, not advisable to cultivate eccentricity in commercial transactions.

By the Bills of Exchange Act, 1882, an indorsement in the case of a bill of exchange, which includes a promissory note and a cheque, always signifies indorsement coupled with delivery, and this transfers the property in it to the transferee, or to the indorsee, if any special indorsee is named. As regards all other documents which are not negotiable, strictly so called, an indorsement does not transfer to the indorsee, or to the person to whom the document is given, any greater rights than those which the transferor possessed.

When any person is under an obligation to indorse a bill of exchange or other instrument, he may indorse it in such a manner, that is, by the addition of words to that effect, as to negative his own personal liability.

By Section 32 of the Act of 1882, the following are the requisites of a valid indorsement—

"(1) It must be written on the bill itself and signed by the indorser. The simple signature of the indorser on the bill, without additional words, is sufficient. An indorsement written on an allonge, or on a 'copy' of a bill issued or negotiated in a country where 'copies' are recognised, is deemed to be written on the bill itself.

"(2) It must be an indorsement of the entire bill. A partial indorsement, that is to say, an indorsement which purports to transfer to the indorsee a part only of the amount payable, or which purports to transfer the bill to two or more indorsees severally, does not operate as a negotiation of the bill.

"(3) Where a bill is payable to the order of two or more payees, or indorsees, who are not partners, all must indorse, unless the one indorsing has authority to indorse for the others.

"(4) Where, in a bill payable to order, the payee or indorsee is wrongly designated, or his name is mis-spelt, he may indorse the bill as therein described, adding, if he thinks fit, his proper signature.

"(5) Where there are two or more indorsements on a bill each indorsement is deemed to have been made in the order in which it appears on the bill, until the contrary is proved."

This matter of order becomes of importance when a bill is dishonoured, for although the holder is entitled, upon giving due notice, to sue any person whose name appears upon the bill, and who has not limited his liability in any way, the person who is thus called upon to pay can only sue any of the parties whose names precede his own, and each of these, in turn, has the right to sue any anterior party. Naturally the holder, if compelled to take legal proceedings, will select as defendant one who is, in his view, most responsible from a financial point of view.

An indorsement may be (1) in blank, (2) special, or (3) restrictive. An indorsement is in blank when the indorser simply signs his name and does not add that of any indorsee. A bill so indorsed becomes payable to bearer. An indorsement is special when a person is named by the indorser to whom, or to whose order, the bill is payable. When there is a special indorsement the bill cannot be further negotiated until the indorsee has signed it. (When a bill has been indorsed in blank, any holder may convert the blank indorsement into a special indorsement by writing above the indorsee's signature a direction to pay the bill to or to the order of himself or some other person.) An indorsement is restrictive when the further negotiation of the bill is prohibited, or when some express direction is given as to the transfer of the ownership thereof, as for example, where the indorsement is "Pay A only," or "Pay A for the account of B," or "Pay A, or order for collection." A restrictive indorsement gives the indorsee the right to receive payment of the bill and to sue any party thereto that his indorser could have sued, but gives him no power to transfer his rights as indorsee unless it expressly authorises him to do so. Where a restrictive indorsement authorises further transfer, all subsequent indorsees take the bill with the same rights and subject to the same liabilities as the first indorsee under the restrictive indorsement.

It only remains to mention the engagements of the indorser of a bill and the estoppels which are binding upon him. The indorser, by the mere fact of indorsement, engages that on due presentment of the bill it shall be accepted and paid according to its tenor, and that if it is dishonoured he will compensate the holder or a subsequent indorser who is compelled to pay it, provided that the requisite proceedings on dishonour are duly taken. He is estopped from denying to a holder in due course the genuineness and regularity in all respects of the drawer's signature and all previous indorsements, and he is further precluded from denying to his immediate or a subsequent indorsee that the bill was at the time of his indorsement a valid and subsisting bill, and that he had then a good title to the same.

INDORSER.

The person who indorses a document. The position and the liabilities of an indorser are sufficiently set out in the article **INDORSEMENT**.

INDUSTRIAL PLANT, REGISTER OF.

(See **DEPRECIATION**, p. 404.)

INFANT.

According to English law a person under the age of twenty-one years, whether male or female, is known as an infant. The twenty-first year is completed on the day preceding the twenty-first birthday, and consequently, since the law takes no account of a portion of a day, any act done even during the first minute of this day preceding the birthday is presumed to be done by an adult.

Primâ facie the nationality and the domicile of an infant depend upon the place of birth, but these may vary with the nationality and the domicile of the parent who has the custody of the infant, provided that the infant does, in fact, change his place of abode.

Up to the age of seven years an infant is not responsible for any criminal act done by him. Between seven and fourteen the liability varies. Of certain offences an infant can never be convicted, and, as to others, a presumption of innocence arises, which can only be removed by clear proof of a malicious intent. In certain cases, however, if an infant is charged with a criminal offence, a parent may be fined if it is proved that sufficient control has not been exercised over the infant. After fourteen, an infant is no more exempt from criminal liability than an adult.

An infant is always personally liable for his torts, and a person who successfully sues him in respect of the same must get what satisfaction he can out of a judgment obtained against the infant.

In contract, however, an infant is not liable except for necessities (*q.v.*), and since the Infant Relief Act, 1874, all contracts made with an infant, (a) for the repayment of money lent or to be lent, (b) for goods supplied, or to be supplied (other than contracts for necessities), and (c) accounts stated, that is, admissions of liability for money due, are absolutely void. By the same Act it is further provided that a ratification, after full age, of any contracts made during infancy, has no binding effect, even if there is a fresh consideration for such ratification. This has given rise to some difficulty in the case of contracts of continuing liability. But it is quite clear, nevertheless, that in such matters as partnership, or the holding of shares in a joint stock company, an infant will be bound after having attained his majority unless he repudiates his liability within a short time of his coming of age. It is to be remembered that an infant is not bound in contract even though he deceives the tradesman

with whom he deals as to his age. The tradesman must take the risk. Without authority, express or implied, an infant cannot bind his parent or guardian, even for necessities. But although he is under no liability, the infant can claim his rights under a contract just in the same manner as an adult can.

In respect of certain special matters the position of an infant is as follows—

(1) **ACTION.**—An infant plaintiff must sue by his "next friend," and an infant defendant must be sued through his "guardian *ad litem*." The next friend is liable for the costs of the action if the plaintiff is unsuccessful. No such liability rests upon the guardian *ad litem*. The only exception to an infant's suing personally is where an action is brought in the County Court by an infant for wages due to him.

(2) **ADMINISTRATION.**—During infancy, if the right to administer a deceased person's estate has devolved upon an infant, the Court will appoint an administrator *durante minore aetate* to act until he attains his majority.

(3) **AGENCY.**—An infant can always act as agent, except that he cannot be proxy for a creditor in bankruptcy proceedings nor for a contributory in winding up a joint stock company.

(4) **BANKRUPTCY.**—The better opinion is that an infant can never be made bankrupt.

(5) **BILLS OF EXCHANGE.**—An infant can never be liable upon a bill of exchange, including a cheque, even though the same is given in respect of necessities supplied.

(6) **COMPANIES.**—An infant may be a member of a joint stock company, and he may sign the memorandum of association. No liability of a pecuniary character attaches to him until he has attained his majority, and he can avoid all liability by repudiating his interest in the company either before coming of age or within a reasonable time afterwards if he has taken no benefit since coming of age.

(7) **EXECUTORSHIP.**—If the person appointed executor under a will is an infant at the date of the testator's death, either the other executors (if any) must act alone during the infant's minority, or the Court must appoint an administrator with the will annexed to act during this period.

(8) **LIMITATION OF ACTIONS.**—The periods of six, twelve, or twenty years do not begin to run against an infant until he has attained his majority.

(9) **PARTNERSHIP.**—Although he may be a partner, an infant is not liable for the partnership debts.

(10) **WILL.**—Unless actually engaged in military service or employed as a mariner at sea, an infant has no testamentary capacity in English law.

The Court exercises a very wide jurisdiction over infants, both as to their custody in the case

of disputes arising between parents, and also as to their property, especially if the property is to fall into possession when the infant attains his or her majority, and if in the meantime provision has to be made as to education, maintenance, and advancement. These matters, however, mainly concern the practice of the Chancery Court.

IN FORMÂ PAUPERIS.

It has been asserted that there was always a right at common law for poor persons to obtain legal aid without expense, if they could satisfy the Court or a judge that they had a good cause of action. At any rate an Act was passed in 1495 by which counsel and solicitors were assigned, under certain conditions, without cost to poor litigants, and this has been known as suing *in formâ pauperis*. The Act just referred to was repealed in 1883, and certain Rules of the Supreme Court dealt with poor persons and their suits. The procedure was not altogether satisfactory, and a drastic change was made in 1914 when new rules came into force. These rules became effective on the 9th June, 1914. This suing *in formâ pauperis* is at present confined to the High Court—it has no application in the County Court at all. Also the right to sue is confined to a Court of first instance. Only under very special circumstances will a suitor be permitted to proceed to the Court of Appeal, and the House of Lords is enabled, under the Appeal (Formâ Pauperis) Act, 1893, to decline to entertain any appeals of this character.

Any person may be admitted to take or to defend, or to be a party to any legal proceedings in the High Court as a poor person on satisfying the Court or a judge that he (or she) has reasonable grounds for taking or defending, or being a party to such proceedings, and that he is not worth £50 (excluding his wearing apparel, tools of trade, and the subject matter of such proceedings) or such larger sum, not exceeding £100, as a judge personally under such circumstances may direct. This rule does not apply to bankruptcy proceedings, nor to any criminal cause or matter except—

(a) Applications to the Court to order a justice or justices to state a case under the Summary Jurisdiction Acts.

(b) The hearing of cases stated under the Summary Jurisdiction Acts.

(c) Applications for certiorari, mandamus, or prohibition directed to a Court of Summary Jurisdiction.

The cases of indigent persons charged with criminal offences are sufficiently provided for by the Poor Prisoners' Defence Act, 1903, so that they do not come within the scope of the new rules at all. It has been stated above that the county courts are left as they were, so far as poor litigants are concerned, although one of the rules provides that "the Court or a judge in considering whether

a person shall be admitted as a poor person under these Rules shall have regard to such statutory provisions as confer on inferior courts concurrent jurisdiction with the High Court, and especially to the provisions of Section 65 and Section 66 of the County Court Act, 1888." These two sections refer to the remission of certain cases which are commenced in the High Court to the County Court.

A new department has been set up at the Law Courts in the Strand for cases in London, whilst for the country the management of the whole business is in the hands of the various District Registrars. The prescribed officers who will attend to the applicants in poor causes are (1) in the Chancery Division, such one or more of the Masters as the Lord Chancellor shall from time to time nominate for that purpose; (2) in the King's Bench Division (excepting on the Crown side), such one or more of the Masters as the Lord Chief Justice shall from time to time nominate, and on the Crown side the Master of the Crown Office for the time being; (3) in the Probate, Divorce, and Admiralty Division, such one or more of the Registrars as the President of the Division shall from time to time nominate; and (4) in a District Registry, as already stated, the District Registrar. It will be the duty of these officials to keep lists of counsel and solicitors who are willing (a) to inquire into and to report upon applications made by poor persons to take or to defend, or be parties to proceedings, and (b) to assist in the conduct of the proceedings themselves. For very obvious reasons the same counsel and solicitors will not be engaged to inquire into the merits of cases and then to carry through the litigious work.

The person desirous of being admitted as a poor person having satisfied himself or herself that he or she is a proper subject for legal aid, will have, first of all, to make a declaration upon a form which will be supplied either in London or at a District Registry, as the case may be, which form must be addressed to the proper official at one or other of these places. The form is as follows—

IN THE HIGH COURT OF JUSTICE.
— DIVISION.

In the matter of an action (or proposed action or other proceeding as the case may be).

[State the parties to the action or proceeding and short particulars of the proposed action or proceeding, and the names and addresses of the persons to whom reference may be made.]

I, the above named _____ of _____ in the County of _____ hereby apply to be admitted as a poor person to prosecute (or defend, or be a party to) the above-mentioned action (or proceeding, or proposed action or proceeding, or state in what respect or

capacity the applicant desires to be admitted as a party to the proceedings), and I declare that I am not worth £50, excluding my wearing apparel and tools of trade, and the subject matter of the action (or proceeding).

(Signed).

To the _____

The application will be referred to one or more of the counsel or solicitors who have put down their names on the list of those who have expressed their willingness to be assigned to inquire into and to report upon cases put forward by poor persons. The inquiries made are of a most stringent character, and the rules afford the utmost latitude for making such inquiries. If the report is unsatisfactory, nothing can be done, at least under the rules. If, on the other hand, the report is favourable, the Court or a judge may, in their or his discretion, and upon such terms, if any, as the Court or judge may think fit, make an order admitting the applicant to take or to defend, or to be a party to legal proceedings as a poor person, and the prescribed officer will assign to the applicant a counsel and a solicitor from amongst those whose names appear upon the panel as willing to act in the conduct of the action or proceedings. As already stated no counsel or solicitor who reports upon the case can be assigned to conduct the action. The case will then take the same course as any proceedings instituted by an ordinary individual. The poor person cannot discharge any counsel or solicitor who has been assigned to him without the leave of the Court or a judge, and, on the other hand, a counsel or a solicitor assigned cannot discontinue assistance unless he satisfies the prescribed officer of the Court, or a judge, that he has some reasonable ground for so discontinuing. It is needless to say that such counsel or solicitor cannot act for any other party in the litigation.

In no case are any court fees payable, and on no account can counsel accept anything, at least at present. The solicitor may receive, either from the poor person or out of any fund which may from time to time be approved by the Lord Chancellor, the payment of out-of-pocket expenses. Until this fund is properly established, the poor litigant will have to find all out-of-pocket expenses, such as the cost of witnesses attending the Court, etc. Naturally all charges will be most carefully scrutinised. If a poor person is successful in his litigation and actually recovers a sum of money or any real or personal property, the money or the property recovered may be charged with the out-of-pocket expenses and, in certain cases, with taxed costs up to one-fourth of the value of what has been recovered. Consequently, the whole procedure amounts to this, that if a poor person has a good cause of action and is recommended as a person whose case should be taken up, he can

now gain admission to the Courts just the same as any other person who is better endowed with the world's goods than he is himself. If the action fails, he loses nothing except what he has had to pay as out of pocket expenses; if the action succeeds, he obtains the whole fruit of the judgment, minus what has just been stated.

INHABITED HOUSE DUTY.

Also called House Tax. This is a tax or duty charged upon inhabited dwelling houses in Great Britain according to their annual value, and payable on or before the 1st January of each year. There have been many cases before the Courts upon the point as to what is and what is not an inhabited house so as to be liable to pay the duty. Generally speaking, the term would seem to embrace all houses in which some person sleeps, all furnished houses ready for use and occupation at any time, even though no person sleeps therein, and all buildings which have internal connections with those parts of the same which are used for residential purposes.

A chamber or apartment in any of the Inns of Court or of Chancery, or in any college or hall in any university, and also a hall or office lawfully chargeable with other taxes or parish rates, are described by statute as inhabited dwelling-houses.

The following premises are exempted from the duty—

(1) Market gardens or nursery grounds occupied by a market gardener or nurseryman *bonâ fide* for the sale of the produce thereof in the way of his trade or business.

(2) Warehouses and buildings on wharves occupied by wharfingers who have dwelling-houses there; also such warehouses as are distinct and separate buildings, not being parts of dwelling-houses or of shops attached, even though adjoining or communicating therewith, but employed for lodging goods or carrying on some manufacture.

(3) Houses belonging to the Crown, and public offices.

(4) Hospitals, charity schools, or houses provided for the relief of poor persons.

(5) Business premises. Where a house is divided structurally and let in different tenements, and any of such tenements are occupied solely for the purpose of any trade, business, profession, or calling by which the occupier seeks a livelihood or profit, or are unoccupied, duty may be charged only on the value of the remaining tenements. Notice must be given to the surveyor of taxes during the year of assessment. Every house or tenement which is so occupied is entitled to exemption, although there may reside on the premises, for the protection thereof, a menial or domestic servant employed by the occupier, or any person of a similar grade or description not otherwise employed by the occupier.

(6) Unoccupied houses or tenements being unfurnished, although left in the charge of persons or servants dwelling therein solely for their protection.

The duty is charged annually on the occupier of the premises. When there is a change of occupation during the year, duty is apportioned according to the time of possession.

When any dwelling-house is divided into different tenements, being distinct properties, every such tenement is chargeable separately on the occupier.

Where any house is let in different storeys, tenements, lodgings, or landings, and is inhabited by two or more persons or families, it is charged in one sum on the landlord. When duty so charged is left unpaid for twenty days, the collector may demand it from or levy for it on any of the tenants, who may in turn make an equivalent deduction from his rent.

Where a house, so far as it is used as a dwelling-house, is used for the sole purpose of providing separate dwellings—

(a) The annual value of any dwelling in the house which is of an annual value below £20 is excluded from the annual value of the house.

(b) The rate in respect of any dwelling in the house of an annual value of £20, but not exceeding £40, is 3d.

(c) The rate in respect of any dwelling in the house of an annual value exceeding £40, but not exceeding £60, is 6d.

The provisions as to (a) and (b) take effect only when a certificate as to suitable and sanitary accommodation is given by the medical officer of health for the district.

There are two scales of duty—the full rate ordinarily charged and the lower rate allowed in certain cases stated hereafter.

The full rates are—

when the annual value is £20, but does not exceed £40—3d. in the £;

when the annual value exceeds £40, but does not exceed £60—6d. in the £;

when the annual value exceeds £60—9d. in the £.

In the lower scale, 2d., 4d., and 6d. are substituted for 3d., 6d., and 9d. respectively in the full scale. The lower rates are allowed to the following premises—

(1) Any dwelling-house occupied by any person in trade, who shall expose to sale and sell any goods, wares, or merchandise in any shop or warehouse being part of the same dwelling-house and in the front, and on the ground or basement story.

(2) Any dwelling-house occupied by any person licensed by law to sell therein, by retail, beer, ale, wine, or other liquors, although the room where such liquors are exposed to sale, sold, drunk, or consumed is not a shop or warehouse. (The

person charged as occupier and the person holding the licence must be identical.)

(3) Any dwelling-house which is a farmhouse occupied by a tenant or farm servant, and *bonâ fide* used for the purpose of husbandry only.

(4) Any dwelling-house occupied by any person who shall carry on therein the business of a hotel-keeper, innkeeper, or coffee-house keeper.

(5) Any dwelling-house occupied by a person for the main purpose of letting furnished lodgings as a means of livelihood. The occupier must register his name with the clerk to the Commissioners of Inland Revenue before the 1st October, and must apply to the Commissioners before the 1st November.

INLAND BILL.

An inland bill of exchange is one that is, or on the face of it purports to be, (a) both drawn and payable within the British Isles, or (b) drawn within the British Islands upon some person resident therein. The British Islands, for the purposes of bills of exchange, mean Great Britain and Ireland, the Isle of Man, the Channel Islands, and the islands adjacent thereto which form a part of His Majesty's Dominions. As it is provided by the Bills of Exchange Act, 1882, that nothing contained therein shall affect the provisions of the Stamp Act, 1870, or Acts amending it, it is important to notice section 36 of the Stamp Act, 1891, which enacts: "A bill or note purporting to be drawn or made out of the United Kingdom is, for the purpose of stamp duty, to be deemed to have been so drawn or made, although it may in fact have been drawn or made within the United Kingdom." It appears, therefore, that for the purposes of stamp duty, a bill which is drawn in, say, the Isle of Man, is regarded as a foreign bill—since the Isle of Man is a place outside the United Kingdom—although it is an inland bill within the definition given in Section 4 of the Bills of Exchange Act, 1882. When an inland bill is indorsed abroad, the indorsement, as regards the payer, is interpreted in accordance with the law of the United Kingdom. Although an inland bill needs no protesting (see BILL OF EXCHANGE, PROTESTING), strictly speaking, this is sometimes done in order to induce a friend of the person liable to come forward and accept the bill for the honour of the person who is so liable. (See also BILL OF EXCHANGE.)

INSPECTION OF DEEDS.

(See AUDITING, p. 96.)

INSTITUTIONS, AUDIT OF.

(See AUDITING, p. 116.)

INSURANCE, BAD DEBTS.

(See BAD AND DOUBTFUL DEBTS RESERVE.)

INSURANCE COMPANIES, AUDIT OF.

(See AUDITING, p. 107.)

INSURANCE DEDUCTIONS, HEALTH AND UNEMPLOYMENT.

(See HEALTH AND UNEMPLOYMENT INSURANCE DEDUCTIONS.)

INSURANCE PREMIUMS.

Premiums due or paid in respect of various classes of insurance should be charged to "Insurance Account." Insurance premiums are payable in advance, and at stocktaking times credit may be taken for the apportioned part of the premiums not accrued due, which as a result will appear on the credit side of the Balance Sheet. The effect of this will be to create an equitable charge for insurance against the period's Profit and Loss Account.

Occasionally it occurs that the risk is carried on for a short period under cover notes, the premiums not being paid by the insured until the policies are prepared. In such cases, where the cover note extends over the period of balancing, there will be an accrued liability to bring into account, and the auditor should make a point of enquiring whether any such liability exists. The auditor should verify the accuracy of all apportionments, and should require the official receipt of the insurance company, or, in the case of the first premium, the policy itself to be produced in support of the amount paid as premium. He should also examine the amounts insured to see that the risks are adequately provided for. (See also AUDITING, pp. 77 and 80.)

INTEREST ACCOUNT.

(See DIVIDEND AND INTEREST ACCOUNT; INTEREST AND DISCOUNT ACCOUNT.)

INTEREST ACCRUED.

(See AUDITING, p. 95.)

INTEREST AND DISCOUNT ACCOUNT.

This account should record only interest on trade debts and on temporary advances (*i.e.* interest not of an annual nature) and the charges incurred in the discounting of unmatured bills receivable. Interest on loans and other annual interest should be charged in a separate account, in order to facilitate the computation of the

assessment of the business to income tax. Cash discounts should also be recorded separately, and should not be confused with the discount on bills, which is in the nature of an interest payment.

Interest and discount, such as should be found in an account of this sort, is of an accruing nature, and, in addition to verifying the charges included in the account by reference to the statements of creditors and bankers and bill brokers, the auditor should see that proper provision is made for any accruing liabilities or interest and discount paid in advance, so that the balance of the account shall only represent an equitable charge for interest and discount for the period under review. (See also DIVIDEND AND INTEREST ACCOUNT.)

INTEREST ON BANK OVER-DRAFTS.

Interest on bank overdrafts should be charged to Interest Account and, subsequently, to Profit and Loss Account. The auditor should verify the charge by reference to the Bank Pass Book and to any other documents, such as agreements with the bank, or letters in which the terms on which interest is payable are set out.

INTEREST ON CALLS PAID IN ADVANCE.

(See PROFIT AND LOSS ACCOUNT, p. 789.)

INTEREST ON CAPITAL AND DRAWINGS.

Interest on capital, which is found chiefly in partnership accounts, is a charge against the profits of the business, and should be credited to the respective partners' Capital Accounts. It forms a means of adjusting the claims of the partners *inter se*, when the capital contributed by them is unequal. Interest on drawings should be debited to the partner's Drawings Accounts, the totals of which are subsequently carried to the debit of the Capital Accounts.

The payment of interest on capital and drawings is dependent on the agreement between the partners. As by the provisions of the Partnership Act of 1890 no interest is chargeable on capital in the absence of an agreement to the contrary, it devolves upon the auditor to ascertain clearly what, if any, agreement between the partners exists upon this matter. For this purpose he should consult the Articles of Partnership, or, where there are no articles, the partners themselves, and thus place himself in a position to determine exactly the terms and conditions under which interest is chargeable on capital and drawings. (See also ADJUSTMENTS AT BALANCING TIME; BALANCE SHEET, p. 148; CONSIGNMENT ACCOUNTS; PARTNERSHIP ACCOUNTS, p. 738.)

INTEREST ON DEBENTURES.

(See PROFIT AND LOSS ACCOUNT, p. 789.)

INTEREST ON DEPOSITS.

(See AUDITING, p. 104.)

INTEREST ON INVESTMENTS.

Interest received from investments should be credited to Profit and Loss Account, through the medium of an Interest on Investments Account. The Investments Ledger should be provided with two columns, one for recording the transactions in the capital amounts of the investments, and the other for recording the revenue arising therefrom. Arrangements should be made whereby authority is given for the interest to be paid direct to the recipient's bankers and not to the investor. The auditor will vouch the interest received by reference to the Bank Pass Book, and the counterpart warrants where such exist. He should in all cases make a point of seeing that the interest is *regularly* received, and any irregularity should be the subject of a strict inquiry. (See also AUDITING, p. 76; BALANCE SHEET, p. 152; PROFIT AND LOSS ACCOUNT, p. 787.)

INTEREST ON LOANS.

(See AUDITING, p. 82; PROFIT AND LOSS ACCOUNT, pp. 787 and 789.)

INTEREST ON MORTGAGES.

(See PROFIT AND LOSS ACCOUNT, pp. 787 and 789.)

INTERIM RECEIVER.

(See BANKRUPTCY ACCOUNTS, p. 179.)

INTERIM TRADING ACCOUNT.

A Trading Account prepared by taking the stock at an approximate figure, without waiting for the usual balancing date.

INTERMEDIATE BALANCING.

A balancing of the books effected during a financial period, an intermediate Profit and Loss Account and Balance Sheet being also sometimes prepared by means of approximation of stock.

INTERMEDIATE LEDGER.

A Ledger through which items may be entered from the subsidiary books, finding their way to the accounts in the principal Ledger to which they are allocatable, by transfer from the Intermediate Ledger.

INTERNAL CHECKS.

The expression internal checks denotes the means by which waste or leakage are controlled, departments linked together, necessary details circulated from one to the other, and information in an

organised form conveyed to the counting-house or book-keeping department to be embodied in what are known as the original books of account. The original books may in their turn be tested by a reference back to the material provided by the system of internal checks, which, it should be added, are quite distinct from such mechanical checks as relate solely to the arithmetical accuracy of the original books themselves.

Internal checks, therefore, serve two distinct functions. They supply and circulate information and they control waste or leakage—the latter, however, within recognised limits. For example, cash or securities can be periodically counted or verified and agreed exactly, and can in any case readily be kept in safe custody. Stocks and stores, on the other hand, are more difficult to control closely, since continuous taking of the whole of large stocks of many varieties, often in bulk, is impracticable, as is also, in many cases, absolutely safe custody. As to labour, precise records of time worked can be kept, but unless employed upon piece work, or work of which the results can be readily measured, the only effectual check upon the proper use of time is personal supervision. In other words, there is no such thing as a complete automatic or mechanical check. In every system of check there is some point at which personal supervision is indispensable.

Internal checks enter into every undertaking, and include the handling of correspondence, recording and dealing with orders and inquiries, the receipt and payment of cash, the receipt and issue of stocks and stores, the despatch of goods, the control of labour and the working out of costs.

The receipt and issue of stocks and stores, the control of labour, and the working out of costs are dealt with in separate articles under those headings. In this article it is proposed to explain the system of internal checks in general use, and then to describe the checks peculiar to such special undertakings as hotels, theatres, railway booking offices and benefit societies. The organisation of departmental stores is dealt with in a separate article (*vide* p. 380). The reader who has mastered the contents of this and the other articles referred to above, should find no trouble in devising a scheme of internal check for any undertaking.

CORRESPONDENCE, ORDERS AND INQUIRIES.—A register for letters should be kept ruled as follows—

Date.	Name.	Address.	Matter.	Date Answered.

All letters received having been opened by a principal (an expression which, whenever used in

this article, is intended to include his duly appointed delegate or a control clerk), should be entered in the register as and when they are opened and at once stamped "Attended to."

"Date....."

They should then be put into baskets (one for each department) labelled "Letters to be replied to," which are handed to the departmental managers for attention. After a letter has been "attended to," it should be initialed by the person who has dealt with it and then placed in a basket labelled "Letters to be filed," a carbon copy of the reply being attached to it, for it is assumed that all letters are typed in duplicate. If a letter has to stand over for any reason, it should be placed in a basket marked "Letters in abeyance." The letters in this basket must be examined daily and cleared up as quickly as possible. The "Letters to be filed" basket should be cleared each evening and the contents put in an alphabetical case of the ordinary type, and the appropriate column in the register of letters marked off showing that the letters have been attended to.

If a letter relates to more than one department copy extracts should be made and passed to the respective departments.

The register should be examined by the principal from time to time in order to see that the letters have been dealt with.

Orders. Copies of all orders, without prices and other private details (and when a general letter includes an order a copy of the part relating to such order), should be typed *in duplicate* on thin paper. Each order should be dated and numbered, and one copy sent to the factory or department concerned, and one copy retained at the office. At the factory or department, and the office, an Order Book should be kept ruled as follows—

Our No.	No. of Order.	Copy of Order (to be pasted in in consecutive order).	Date recd.	Estimated date of completion	Date completed.	Date Delivered.	No. of Delivery Order.
	Customer's No.						

As to orders received by telephone or word of mouth, particulars should be typed and dealt with in the same way.

In factories where there are several processes necessary to make the finished article, instructions for the factory should be made out on numbered tickets in duplicate. The original ticket is retained in the office. The other is detached and sent to department No. 1. This ticket follows the order from department to department till it reaches the warehouse with the

finished article, where it is marked off against the original order in the counterfoil book.

Where work is commenced simultaneously on one order in more than one department tickets are sent to each of these departments and circulated until they finally meet at a point in the manufacture whence they reach the warehouse as before.

The principal should examine the Order Book from day to day and follow up orders which are in arrear.

Inquiries. The same procedure, so far as appropriate, should be adopted, as in the case of letters or orders, and Inquiry Books suitably ruled should be kept.

The original orders and inquiries, and correspondence relating thereto, are filed in alphabetical cases, labelled "orders" and "inquiries" respectively.

The Inquiry Book should also be inspected by the principal periodically.

Letters Outwards. All letters sent out should be recorded in a Register ruled as follows—

Date.	Name.	Address.	Matter.	Postage, if any.

The postage should be totalled daily or weekly and entered in the Petty Cash Book. For the purpose of agreeing the petty cash, stamps on hand may be treated as "cash."

Receipt of Cash. Cash may be received—

- By post.
- Across the counter.
- Through travellers or collectors.

(a) **RECEIPTS BY POST.** As the letters are opened (see above) the principal should make a note on each letter covering a remittance, of the nature and the amount of the remittance—whether an acceptance, cheque, postal order, notes, cash or traveller's remittance. He should at the same time jot down the name of those remitting and the amounts on a rough slip of paper and total up same for use as mentioned below. All uncrossed cheques and postal orders should at once be crossed by means of a rubber stamp such as the following—

*Bank of England
a/c John Smith & Co., Ltd.*

The remittances and covering letters are then handed to the cashier, who at once enters the necessary details in his Cash Received Book, fills up the paying-in slip in the Bank Paying-in Book,

and pays the total into the bank. The bank cashier stamps the counterfoil paying-in slip as correct. The principal compares the rough slip referred to above with the Cash Book and counterfoil paying-in slip as stamped by the bank, and periodically agrees the amount in the Bank Pass Book itself with the paying-in slip.

Counterfoil receipts numbered in consecutive order, and stamped where necessary, are made out by a receipts clerk, who enters the Cash Book folio on the counterfoil of the receipt, and the number of the receipt in a column in the Cash Received Book, and also compares his receipts with the covering letters (if any) sent out, and with the principal's rough note referred to above.

The principal must see that acceptances received are entered by the bills clerk in the Bills Receivable Book, and if discounted, duly entered in the Cash Book. The date of discounting and the Cash Book folio should also be entered in the Bill Book, which in practice usually serves as a ledger as well as a record for bills receivable, and should be suitably ruled for that purpose. The principal should periodically agree the balance of the Bills Receivable Account with the bills on hand. For receipts by letter delivered by hand the same routine should be observed. The principal's rough list duly followed up is the best safeguard against irregularities.

RECEIPTS THROUGH TRAVELLERS. It is better that all monies should be remitted direct to the head-office by customers, but it is often convenient to utilise the traveller also as a collector, especially in the case of dilatory accounts. The traveller should be furnished with a list of the accounts to be collected on his journey, a duplicate being retained by the principal. The traveller should also be given a counterfoil receipt book containing official forms of receipt numbered consecutively and duly stamped.

If there are many small items below £2 to collect he may also be given a counterfoil Receipt Book with unstamped receipts. The receipt should bear a note to the effect that no other form of receipt will be recognised, and a similar note should be impressed upon all invoices and statements of account.

The traveller, on collecting money, must give one of the official receipts from the counterfoil book, entering full particulars on the counterfoil.

Each evening the traveller must forward all cheques collected and a remittance for cash received, accompanied by a report with suitable details. Arrangements can usually be made by which he pays in monies to a local bank, for transmission to the Banking Account of his head office. In this case he sends a duplicate paying-in slip, duly initialed, with a report as before. He must not use the cash collected for his travelling expenses.

From the traveller's report the principal marks off on the list referred to above, the accounts collected, and may, if advisable, send a reminder to those who have not paid. The unpaid items on the list should be entered on a list to be handed to the traveller when going again on the same journey.

Once a month or oftener the ledger clerk should hand to the principal a list of accounts in arrear, distinguishing those accounts which have been entrusted to the traveller for collection. Those accounts should be carefully scrutinised and inquiries made.

It should be the duty of a ledger clerk to look through the trade journals, which publish particulars of judgments, receiving orders, and so forth, and at once notify the principal if any of the firm's customers are at fault, and record the facts on the margin of the customer's Ledger Account.

PAYMENTS OF CASH.—Payments may relate to—

- (1) Monthly statements.
- (2) Salaries.
- (3) Wages.
- (4) Customs.
- (5) Directors' fees.
- (6) Taxes.
- (7) Petty cash.

As to items 1, 5 and 6, payment should be made by cheque crossed "Account Payee only." The name of the payee's banker, if known, should be added to the crossing, which might then be as follows—

*Account Payee only.
Bank of England.*

Cheques so crossed can only be cleared through the payee's account at his bank, and the risk of irregularities is obviated.

The monthly statements are a summary of the invoices for the month. They are usually passed for payment by the Bought Ledger clerk. This implies that he has compared the amounts on the statement with the invoices; that correct allowances have been made for trade and cash discounts and returns and that the additions and extensions are correct. The statement is impressed by means of a rubber stamp as follows—

"Compared with invoices and credit notes.

Discounts checked. Additions checked.

Agreed with Ledger (folio).

Passed for payment."

The clerk responsible for each section of the

checking puts his initials against same on the form given above. The invoices themselves are checked by the invoice clerk in the following way: For each delivery of goods an advice note is received giving the particulars of weights and quantities, but no prices. This is verified by the store-keeper, and passed on to the invoice clerk, who places all advice notes passed on to him in an alphabetical case labelled "Advice notes awaiting invoices." The invoices when received are immediately impressed with a rubber stamp as follows—

"Quantities and weight correct.

"Prices.

"Additions and extensions.

"Trade discount."

The invoice clerk compares the invoice with the advice note, files away the advice note (thus clearing the alphabetical case) agrees the prices with the original order, the number of which should always be stated on the advice note, checks the discounts, additions and extensions, putting his initials in the proper place, and then files the invoices in an alphabetical case marked "Invoices awaiting monthly statements." As mentioned above the invoices are agreed with the monthly statements when received, and pinned to the statements. A list of amounts payable is then made out and handed to the cashier, who draws the cheques and submits same to his principal, who compares them with the lists and statements. Monthly, weekly, or daily, if necessary, all invoices are entered up in the Bought Day Book by the invoice clerk and posted therefrom to the Bought Ledger by the Bought Ledger clerk, who, as already mentioned, compares the statements with his ledger. The amounts of the cheques drawn in payment are periodically posted to the Ledger by him and the account ruled off. He thus becomes responsible for seeing that the cheques drawn are for the proper amount and no more.

The payments in the Cash Book should be numbered in consecutive order, and it should be the duty of a clerk to see that vouchers are duly received for all payments recorded in the Cash Book, and that they are numbered to correspond with the Cash Book entries and filed in that order.

The cashier must not be allowed to make any entries in the ledgers, and the Bought Ledger clerk must not be allowed to pay any accounts, whether by cheque or by cash. The whole of the work should, from time to time, be independently checked by the principal or by an independent control clerk.

If the books be balanced by a chartered accountant on the system described in the article under the heading BOOKS, BALANCING OF, a further element of independent check is introduced.

Salaries. A Salaries Book should be kept showing each month or week the names of the salaried staff and the amount payable to them. This should be verified by the principal and signed by him as correct, and a cheque drawn and signed accordingly. Payment should be made by the principal personally or by his delegate.

Wages. See CONTROL OF LABOUR, p. 564.

Customs. Customs Duties are paid by Bank of England cheque to bearer or by cash, and no receipts are given. Particulars, duly verified independently of the cashier, should be submitted to the principal and signed by him when he signs the cheques and filed as a voucher.

DISPATCH OF GOODS.—The dispatch of goods is handled by the dispatch department. When goods are ready for delivery the dispatch clerk makes out an advice note in triplicate giving a description of the goods, the weights or quantities, but no prices. The advice note may be in the following form—

From A. B. COMPANY, LTD.,
VULCAN WORKS,
LONDON.

-----19..

Advice Note No.-----

To X. Y. Z. & Co.,

SPRING STREET,

LEEDS.

Please receive per Great Northern Railway,

For A. B. & Co., Ltd.

Your Order No.-----

Our " "-----

One copy of the advice note is given to the gate-keeper, who has instructions to allow nothing to leave the works without written authority from the dispatch department. This he signs and passes on to the office. One copy is posted to the customer, or accompanies the goods if they are delivered direct by the seller. From the counterfoils of the advice notes which are sent to him for the purpose, the invoice clerk makes out and posts to the customer the invoice, on which he quotes the number of the advice notes. The corresponding order in the Order Book is also marked off from the advice note counterfoil. The invoice

is followed up by a monthly statement. The manager can therefore follow the order from the Order Book through the works to the despatch department, and finally to the customers' Ledger Account.

In addition to the safeguards provided by the usual internal checks, all employees collecting or handling cash or securities should be duly guaranteed by an insurance company's Guarantee Policy. The conditions of the policy must be strictly observed.

INTERNAL CHECKS APPLIED TO HOTELS.—

The object of internal checks in the case of hotels is to see that the visitors are duly charged with all that they should be, whether rooms, baths, fires, meals, or refreshments.

Rooms. As regards the letting of rooms, the reception office clerk enters the rooms let, distinguished by numbers, in memorandum books, which go at frequent intervals to the cashier's office to be entered in the Hotel Day Books.

The Day Books are in the form of a Tabular Ledger into which the charges against each visitor are entered direct, under his room number. In this way the visitors' accounts are always kept closely written up in detail and a bill may be made out any time at short notice. The entries in the Day Books are continuously checked off with the reception office Day Books by control clerks.

Baths. For baths a duplicate check is made out by the chambermaid and sent to the cashier's office.

Fires. For fires in visitors' rooms, a duplicate check is made out by the housekeeper and sent to the cashier's office.

Meals. For meals served in public rooms the waiter, on taking the visitor's order, asks for the number of his room, and then makes out a check in duplicate for the visitor's requirements. The requirements from the kitchen, cellar or store must be on separate checks, usually of distinctive colours. If the visitor is one of a party, the waiter inserts on the order the number of persons. The check is shown to the coffee room or restaurant clerk, who stamps it and enters short particulars in a Columnar Book before the check is taken to the kitchen. Of the duplicate check, one part goes to the cashier's office for entry in the Day Book and the other to the kitchen, cellar or store, as the case may be. The coffee room or restaurant clerk's Columnar Book is sent to the cashier's office after each meal, written up in the Day Books, and in due course compared with the checks.

Nothing is issued from the kitchen, cellar or store except in exchange for a check. From these checks the stores clerks record what is issued, for which the checks received are a voucher.

For meals served in visitors' rooms a check is sent by the head waiter to the cashier's office.

The whole of the checks are continuously controlled by control clerks and agreed with the kitchen, cellar or store records and those of the cashier's office, including the Day Books. The control clerks see that the amounts are duly entered up and accounted for either by a charge to the visitor or by cash. The purchases for kitchen, cellar or stores, as per the delivery notes received from the suppliers, are also checked by the control clerks. Cigar and cellar stocks are checked at least once a month. Bar stocks and general stocks are checked weekly, or oftener if required. The visitors' accounts in the Tabular Ledger are also controlled by the control clerks and the cash credited in settlement agreed with the Cash Book.

Kitchen. The manager informs the chef how many visitors he considers it necessary to provide for at each meal and keeps a record showing from day to day the percentage the consumption of food bears to the meals served as per the checks. This gives a rough control as regards waste or leakage in the kitchen. An exact check upon the kitchen is, under the circumstances, impossible, but the supervision of the manager, added to the percentage test, is usually a sufficient check.

Payment of Bills. The hotel porter does not permit visitor's luggage to be removed from any room until he has received a check from the cashier's office indicating that the visitor's bill has been paid. In some cases these checks take the form of a hotel label, which, when fixed to the visitor's luggage, indicates that the visitor has paid his bill. It will be seen that a continuous independent check is constantly going on, and at the same time the necessary book-keeping details are quickly provided, which in the case of a hotel is absolutely essential.

INTERNAL CHECKS APPLIED TO THEATRES.

—The income of a theatre is derived from—

- (1) Bookings in respect of reserved seats, viz—
 - (a) Advanced bookings by the box office.
 - (b) Cash bookings by the box office.
 - (c) Library bookings by the libraries.
- (2) Cash taken at the doors for unreserved seats.
- (3) Sales of programmes.
- (4) Advertisements in programmes.
- (5) Cloak-room fees.
- (6) Bar takings.

The system of internal checks adopted is as follows—

(1) **Reserved Bookings.** The box office is furnished with a plan of the house and a set of tickets for each performance. The plan (which has the date of the performance impressed upon it), shows the seating capacity of the theatre. Each row of seats is distinguished by a letter or number, and each seat by a number. The tickets are lettered and numbered to correspond

with the plan, and are in four parts, bound in book form. The usual form is as below—

1	2	3	4
Stalls Saturday March 9th Evening Row D 2	Stalls Saturday March 9th Evening Row D 2	Stalls Saturday March 9th Evening Row D 2	Stalls Saturday March 9th Evening Row D 2

In the case of box-office bookings, parts 3 and 4 are given to the patron. If the ticket be for an advance performance the box-office clerk tears out part 2 and files it in order of date. The patron on entering the theatre gives the ticket to the check-taker, who retains part 4 and returns part 3 to the patron. Part 4 is deposited in a lock-up receptacle by the check-taker, who himself has nothing whatever to do with the box-office. From the contents of the receptacle a control clerk makes a return to the acting manager in the following form—

COUNTER'S RETURN

Date _____ 19____

Tickets.	Total.	Booking.	Libraries.	Compts.
	£ s. d.	£ s. d.	£ s. d.	£ s. d.
Stalls at Dress Circle, at "Upper", at "Complimentary"				
Total				

PROGRAMMES

Issued	.	.	.
Returned	.	.	.
Sold	.	.	.

As soon as the seat is sold, the corresponding seat in the plan is marked off on the plan to which it relates; this must be done with the most scrupulous accuracy.

Where tickets are sold by the libraries (which frequently use their own tickets, filling in the particulars as obtained from the box office by telephone), the box-office clerk on marking the plan uses a special mark, and puts the initial of the library against the seats so booked. The

MATURED BOOKINGS

Date_____ 19____						
				£	s.	d.
Private Boxes	.	.	at			
"	"	.	at			
Stalls	.	.	at			
Dress Circle	.	.	at			
Seat in Boxes	.	.	at			
Upper Circle	.	.	at			
"	"	.	at			
				£		

RETURN FROM UPPER CIRCLE

Date_____ 19____						
				£	s.	d.
Sold	.	.	at			
Sold	.	.	at			
TRANSFERS FROM PIT.						
Sold	.	.	at			
Sold	.	.	at			
TRANSFERS FROM GALLERY.						
Sold	.	.	at			
Sold	.	.	at			
				£		
Notes—						
Fives				£		
One				£		
10s.				£		
Silver				£		
Signed_____						

These are duly verified by the control clerk by reference to the plans and tickets.

(2) **Unreserved Seats.** The check upon unreserved seats is of a simpler nature; check machines or roll tickets are used. In the former case the machine automatically records the tickets sold; in the latter, the number of the tickets are a sufficient check. A return is also made of these takings and in the following form—

RETURN FROM PIT

Date_____ 19____						
				£	s.	d.
No. Finish						
No. Begin						
Sold			at			
TRANSFERS FROM GALLERY.						
No. Finish						
No. Begin						
Sold			at			
				£		
Notes—						
Fives				£		
One				£		
10s.				£		
Silver				£		
Signed_____						

RETURN FROM GALLERY

Date_____ 19____						
				£	s.	d.
No. Finish						
No. Begin						
Sold			at			
				£		
Notes—						
Fives				£		
One				£		
10s.				£		
Silver				£		
Signed_____						

The cash takings as a whole are summarised in the following form—

SUMMARY OF CASH

Date_____ 19____						
				£	s.	d.
Booking						
Doors						
Notes—						
Fives						
One						
10s.						
Silver						
Cheques						
M.O.						
P.O.O.						
				£		

The total, as shown by the Summary, should agree with the total cash banked, and the control clerk must see that it does. Where re-admission is permitted a special form of check is issued ; this should be varied in form or colour from performance to performance. Transfers to higher-priced seats are dealt with by issue of a new ticket. The proceeds of the new ticket are accounted for by the box-office clerk, or, in the case of unreserved seats, by the person responsible therefor, partly by cash, and partly by the pass-out check issued to the patron. A summary is finally made in the following form—

FINAL SUMMARY									
----- 19-----									
Performance No.									
		£	s.	d.	£	s.	d.		
Booking . .									
Libraries . .									
Front Doors . .									
Upper Circle . .									
Pit . .									
Gallery . .									

This form may be checked by an inspection of the tickets in the box-office, after deducting complimentary seats and the records relating to the unreserved seats.

The control clerk sees that the libraries are correctly charged up, the accounts rendered monthly, and duly collected.

(3) **Sales of Programmes.** A certain number of programmes, each bound with a wrapper of some sort, are printed and delivered at the theatre ; the number delivered being duly certified by the printer. Each theatre attendant is given so many programmes for which he or she has to account in cash or in programmes returned with unbroken wrappers.

(4) **Advertisements in Programmes.** A register of programme advertisements should be kept giving full particulars, for which purpose each advertisement should be given a distinctive number. This distinctive number is printed below the advertisement on the programme. The control clerk must see that each advertisement on the programme is numbered, trace same to the register of advertisements, and see that it is duly charged up and ultimately collected.

(5) **Cloakroom Fees.** A book of numbered counterfoil tickets, each ticket bearing the amount of the fee chargeable should be used. The ticket is handed to the patron, and handed back by him on his claiming the article deposited. A control clerk agrees the cash with the counterfoils, and with a summary made by the cloakroom attendant.

(6) **Bar Takings.** Each bar attendant makes a return of her takings in a form such as the following—

RETURN BY BAR ATTENDANT'

Date----- 19-----

Stalls—		£	s.	d.
Matinee				
Evening				
Programmes—	£			
No.				
----- Matinee				
----- Evening				

Signature of Manager.				

Signature of Attendant.				

Each waiter or waitress makes a return in the following form—

RETURN BY WAITER OR WAITRESS

Date-----

Sales.	£	s.	d.
Programmes—			
Matinee			
Evening			
Chocolates—			
Matinee			
Evening			
Minerals—			
Matinee			
Evening			
Tea and Coffee—			
Matinee			
Evening			
Sundries—			
Matinee			
Evening			
		£	

Signature of Waiter or Waitress.			

Manager.			

The manager, on taking the cash from the attendants, initials the forms, and makes up a final summary, as follows—

RETURN BY BAR MANAGER

Date_____ 19____

	£	s.	d.
Stalls			
Dress Circle			
Upper Circle			
Pit			
Gallery			
	£		

Programme

Number.
£

Signature of Manager.

The control clerk sees that the cash agrees with the particulars on the various forms, and that it has been duly banked. The stock is taken at least once a month by professional gaugers who prepare statements from which the receipts to be accounted for can be deduced, and this is compared with the cash.

The whole of the takings, other than from advertisements on programmes, are summarised in form shown in the next column—

This is carefully verified by the control clerk by reference to all the various forms and returns given above, and by reference to the bank paying-in slip and the Bank Pass Book.

The foregoing comprise that part of the internal checks in a theatre which, except as regards bar takings, is peculiar to theatres and enterprises of a similar nature.

INTERNAL CHECKS APPLIED TO RAILWAY AND STEAMSHIP BOOKING AGENCIES.—The agency business, carried on under stringent agreements by these agencies for their principals, the leading railway and steamship companies, is practically a cash business, a remittance by the agencies for tickets sold being made to the railway companies monthly or weekly, according to the tenor of the agreements.

In the case of shipping companies, payment, *less commission allowed*, is required from the agencies in exchange for each booking.

RECEIPTS. WEEK ENDED

Day.	Total House.	Libraries.	Matur'd Bookings.	Cash.	Advance Bookings.	Remit'd by Libraries.	No. of Progs.	Programmes.	Bars.	Cloak Rooms.	Total Banked.	Notes.
Monday												
Tuesday												
Wednesday												
Thursday												
Friday												
Saturday, M.												
" E.												

LIBRARIES.

Balance from last week

Add—Bookings as above

Deduct—Cash as above

Owing

ADVANCE BOOKING.

Forward from last week

Advance booking as above

Deduct—Matured booking as above

Balance

In the case of railway companies, the almost invariable rule is to forbid any deductions from the receipts for tickets, and to settle the agreed commission quarterly or half-yearly.

The object of internal checks in the case of such agencies is to ensure that every ticket sold is accounted for, and that the unsold tickets are actually on hand, for which purpose the following procedure should be adopted: A separate Banking Account must be kept by the agencies for receipts on account of principals; which, since the steamship transactions are on a cash footing, means in practice for the railway companies. A Tickets Sold or "Train" Book is kept for each railway company, in which are entered full details of the tickets sold each day—

amount at the bank, less any payments made on account. The control clerk satisfies himself that these figures do agree and sees the railway office receipt for payments made to them. The foregoing totals are again checked by reference to a elaborately detailed summary of the tickets sold for each company, which has to be prepared and sent to the railway companies at the close of each month.

The accuracy of this summary is also verified by the control clerk, who, in addition, takes stock of the railway tickets on hand. By deducting the total stock from the statement of tickets delivered to the agency by the companies, he is able to put an absolute check upon the quantities of tickets sold. A further check is supplied by the fact that the representatives of the railway

TRAIN BOOK

Date.	Stations.	Description of Ticket.	Commencing Number.	Closing Number.	No. of Passengers.						Rate.	Amount.	Daily Totals.			
					Single.			Return.								
					1	2	3	1	2	3						

The total of each Memorandum Book is carried to the credit of the various railway companies in a columnar Railway Ledger (p. 563).

The daily total of the cross casts of the columns in the Ledger represents the value of the tickets sold during the day. This total is posted to the debit side of the Railway Counter Cash Book (p. 563).

It will be observed that the Railway Counter Cash Book (which is frequently called the Till Book), although relating in the first place only to receipts, has debit and credit columns. This is to meet cases in which railway tickets are not used and are handed back to the office in exchange for cash, thereby reducing the amount payable to the principals. The balance of this cash book at the close of each day should correspond with the cash in the till, which is paid into the separate Banking Account referred to above. The Cash Book and the bank paying-in slip, and eventually the Bank Pass Book, are compared and agreed by a control clerk. The control clerk also agrees the total of the sums carried daily into the Railway Counter Cash Book with the totals due to the railway companies, as shown by the Columnar Ledger. The final totals of both these books (less the value of any cancelled tickets taken back by the agency) represent the amounts payable to the railway companies, as well as the

companies attend from time to time to make an inspection of the tickets on hand, and agree the results with their records.

INTERNAL CHECKS APPLIED TO MUTUAL BENEFIT SOCIETIES.—In certain classes of such societies where benefits cannot be obtained except on the production of a membership ticket it is possible to make provision for a most effective internal check upon the receipts in respect of subscriptions. The method adopted is as follows: The membership tickets are numbered consecutively and either bound up in counterfoil books, or, if that be inconvenient owing to the nature of the ticket, they may be loose but with flimsy counterfoils attached. There is printed on the ticket the year for which it is available and the subscription payable. The name of the member is written in, indelible ink being used. The colours of the tickets are changed each year. The society's stationer prints and delivers a specified number of tickets each year, sending direct to the control clerk a certificate of the number so printed, giving the commencing and finishing numbers of the tickets. A committee of the society certify to the total number of members of each class to any given date. The Cash Book which is written up from the counterfoils of the tickets issued, is on the columnar plan with columns for each class of

RAILWAY LEDGER

[illegible]

RAILWAY COUNTER CASH BOOK

RAILWAY COUNTER CASH BOOK													Cr.
Dr.													
19													
Jan. 1	To Railway Tickets F. Robinson, Deposit, 7s S.S. "Asprey"	R.L. 16	47	6	1	19 Jan. 1	By Cancelled. " Bank Cash Book.	G.W.R. G.N.R.	R.L. 16 " 1	1 48	6 11 6	3 4 6	
			3							50	6	1	
			50	6	1								
Jan. 2	To Railway Tickets	R.L. 16	43	1	5	Jan. 2	By Cancelled. " " " Bank Cash Book.	L. & N.W.R. G.N.R. G.E.R.	R.L. 16 " 1	1 41	3 6 5	1 4 3	
			43	1	5					43	1	5	

INT]

THE ACCOUNTANT'S DICTIONARY

[INT

(FLIMSY)

Reverse of Flimsy Ticket

Let go before Stamping

WORK TICKET No.---

No.

THIS SIDE TOWARD YOU

Don't Use Force

Charge to _____ a/c _____ Work Ticket No. _____		Job No. _____	
Symbol No. _____	Drwg. No. _____	Number Off. _____	
Description _____			
Operation _____			

QUANTITIES CERTIFIED.		Accepted		Rejected		Certified	
Clock No.	NAME.	Mach. No.	Date.	Quantity.	Initials.	TOTAL	

[illegible]

(NOTE.—The flimsy is detached and kept in the Costs Office, as explained on page 572.)

INT]

THE ACCOUNTANT'S DICTIONARY

[INT

APPLICATION AND ENGAGEMENT FORM

To be filled in by Applicant

Name ----- Age -----

Address -----

PREVIOUS EXPERIENCE

Name of Employer.	Address of Employer.	Capacity.	Clock No.	Foreman's Name.	Rate.	Length of Service.	Date of Leaving.	Reason for Leaving.

State Union (if any) -----

Date ----- Signature of Applicant -----

To be filled in by Interviewer

General Impression formed -----

Capacity in which it is proposed to engage applicant if Refs. satisfactory -----

----- Rate ----- per hour.

To start ----- Date ----- Signed -----

To be filled in by Office

References applied for, from -----

on ----- Replies received and

passed by ----- Date -----

Started ----- Clock No. -----

INSURANCE AND UNEMPLOYMENT ACTS		CHECK No.
Full Name (Surname first)_____		No. of Contribution Card.
Full Postal Address _____		

THE FIRM REQUESTS ADVICE OF ALTERATION IN ADDRESS OF ANY EMPLOYEE

Age last Birthday_____	Date of last Birthday_____
Dept. Employed_____	Capacity_____

FOR OFFICE USE.						Code Letter
If Exempt or Exception state Cause. }	_____					

Under 16 yrs. Health or apprentice, etc., exempt. unemp.	16-21 yrs. Health or 16-18 yrs. unemp.	Over 21 yrs. Health or over 18 yrs. unemp.	Rate of Wages.	Employee's Contribution.	Firm's Contribution.	Date of Card.

Reverse Side.

Name_____						CHECK No.
Address.			Recommended by			
_____			_____			
_____			_____			
Entered Employ.			Salary Started.	Increases.		
Married.	Single.	Left Employ.	Reason for Leaving.			

Remarks :

Book is entered up accordingly. The quantities are also recorded by the stores or warehouse clerks.

Separate records are also made of overtime, so as to show from week to week how much overtime is being worked and so prevent abuse. A separate record is also made of late arrivals and absentees.

From the works tickets abstracts are prepared for costing purposes. Where tickets are not used the workman is sometimes given a small book in which to record his time. This is initialed by the foreman and forms the basis of the abstract of cost. In all departments where highly skilled labour is employed and wages are high, a system of departmental time recording is adopted, so as to obviate waste of time due to delay between the completion of one job and the commencement of another. The system is as follows: A separate clock is installed, together with card cases, in the department. The cards used are as follows—

In the first place the foreman picks out for each workman two or three jobs in advance, according to the orders he has in hand and the suitability of the workman to do the work on these orders. The orders are written out and put into the employee's card case (see Job Ticket, page 568). As soon as he has finished a job he goes to his card case and takes the next job in succession and proceeds with it forthwith. Should the foreman, for a breakdown job, have to stop a man on a certain order which he is doing, he himself takes the particular breakdown order to the workman and the latter immediately "clocks out" on the job he is working on, returning the card to its division in the card case as a suspended job and clocking on to another card given him by the foreman. To allow the foreman a certain amount of latitude, certain stock orders for dies, punches, extractors, etc., which are being constantly used, are put down as stock jobs or orders to an individual. (See Stock Order Card, on page 569.) These stock order cards remain in the workman's card case until he has worked off the quantity required on the order, and serve as a secondary job on which a man can always fall back in case of no orders coming from his foreman to keep him employed. When any one of these tickets is filled up, a supplementary work ticket is issued to the workman upon which to carry on the record. (See notes on tickets as above.)

By this system a considerable amount of time is saved. The foreman practically keeps his shop going automatically, having plenty of time to supervise the finish of the work and also to arrange systematically the giving out of his orders. He can also at any time, by going to the card case, find out what jobs are completed. The cards are immediately extracted and returned to the

works office to enable the works clerks to proceed with the costing of the particular job in question.

A duplicate card on flimsy paper, called a flimsy, is frequently attached to the cards. The flimsy is detached after the card is issued and kept in the cost office and written up from day to day by reference to the card itself. This avoids taking the card away from the control of the workman while at work.

In abstracting the time, any time lost should be summarised under a separate heading.

The wages sheets may also be independently tested as to rates and the number employed by reference to the file of workmen's application and engagement forms and insurance records, which are shown on pages 570, 571.

The application and engagement form explains itself. As to the Insurance Record card, the application and engagement forms, when completed, are returned to the works office for filing, and from the particulars given the "Insurance Record Card" is made out, showing the employee's name, address and age, and whether insurable or not. If an employee is not insurable at time of entering employ, discs are provided which indicate on the Insurance Record card the year and quarter of the year when they will become insurable. (See also AUDITING, p. 75; FRAUD AND FALSIFICATION OF ACCOUNTS, p. 507; INVESTIGATIONS, p. 585; OFFICE ORGANISATION AND SCHEMES OF INTERNAL CHECK.)

INTER VIVOS GIFTS.

(See EXECUTORSHIP ACCOUNTS.)

INTESTATE'S ESTATE, AUDIT OF.

(See Auditing, p. 67.)

INTROMISSION.

This is a term used in Scotch law, signifying the assumption of authority on the part of one person to deal with the property of another.

INVENTORY.

Any list of articles or goods. The law requires that an inventory shall be attached to certain special documents, and in other cases an inventory is found advantageous for reference or comparison. Thus, an inventory is always attached to a bill of sale, a hire-purchase agreement, a marriage settlement, etc. When a distress (*q.v.*) is levied, an inventory must always be made of the goods and chattels which are seized. Again, an executor or an administrator must always make a "complete list or inventory of all the goods, chattels, wares, and merchandise of the deceased person whose estate is entrusted to his care for administration. And lastly, when a furnished house is let, it is the invariable practice for the parties to draw up an inventory in duplicate, so that a settlement may be arrived at when the tenancy terminates.

INVESTIGATIONS.

DEFINITION. An investigation is an examination of and inquiry into the records of past transactions with a view to disclosing the true position of affairs in respect of matters falling within the scope of the inquiry.

Most of the work of a professional accountant falls into one of two categories, accountancy and auditing. Accountancy is of a constructive nature and consists in the building up of accounts and records, whereas auditing is of a critical nature and consists of an examination of accounts and records already prepared. An investigation usually involves both accountancy and auditing work.

THE NATURE OF AN INVESTIGATION.—An investigation is to a certain extent analogous to an audit, but, as has just been pointed out, it will, as a rule, involve accountancy work in addition.

In the case of an audit the object is to verify the Balance Sheet of the business or concern in order to determine whether or not it shows the true position of affairs. The auditor commences his examination as a rule without definite instructions, and with no object in view otherwise than proving the accuracy of the records for the particular year. He starts his work without prejudice or suspicion of any kind, yet performs his duties, if he be a wise man, without placing undue trust or confidence in any person whose records he has to examine.

An investigation aims at the discovery of facts which as a rule can only be ascertained as the result of the investigation, and it is desirable that the investigator should always have his mind open to every suspicious circumstance, and if necessary go out of his way to allow his suspicions to be aroused, since by so doing he will best serve his clients.

THE ESSENTIAL QUALIFICATIONS OF AN INVESTIGATOR.—In no branch of the accountants' profession is there more necessity for skill and judgment than in the conduct of an investigation.

The investigator must have thorough knowledge of the principles underlying book-keeping, accounts and auditing, and for this reason a professional accountant alone is competent to carry out these onerous duties. He must be able to reason well, and should have studied the various frauds which have come before the public eye from time to time. Above all, he must, to be successful, be a student of human nature, for all investigations, whether they involve fraud or otherwise, are necessitated by the fact that human nature is what it is. He must also be competent, tactful, and courteous, and particularly careful in his operations, his conclusions, and his pronouncements.

THE SUBJECT MATTER OF INVESTIGATIONS.—Any transaction, or set of transactions, can be the subject of an investigation, and there is practically no limit to the special cases in which an investigation may be called for. An investigation is equally applicable to the fraud involving hundreds of thousands of pounds, as it is to a peculation of petty cash or of postage stamps, by means of false entries in the postage book; and where one man is a buyer and another is a seller, the determination of a fair value of goodwill is equally desirable in the case of a large and valuable concern, as in the case of a small business. Again, if one man be a borrower and another a lender, it is equally important to the lender to ascertain the true state of affairs of the borrower; whether he be a man of known integrity and business worth or whether little or nothing is known of him.

As there are so many cases which may be left to the arbitrament of the investigator, it is proposed to deal here with various specific cases as follows—

(a) An investigation of the accounts of a business which it is proposed to transfer to a limited company, with a view to the certification of the profits for the prospectus.

(b) An investigation on behalf of a private individual or firm about to purchase a business.

(c) An investigation on behalf of a person who is proposing to take a partnership in a going concern.

(d) An investigation on behalf of an individual or firm proposing to finance a business by advancing money to the proprietors, or taking up shares or debentures in a private company.

(e) An investigation on behalf of a shareholders' committee.

(f) An investigation on behalf of the proprietors of a business into a known or suspected fraud.

(g) An investigation under the Public Trustee Act, 1906.

AN INVESTIGATION OF THE ACCOUNTS OF A BUSINESS WHICH IT IS PROPOSED TO TRANSFER TO A LIMITED COMPANY, WITH A VIEW TO THE CERTIFICATION OF PROFITS FOR A PROSPECTUS.—(a) **Preliminary Requirements.**

The investigator will require an express contract with his employer as a condition precedent to making the investigation. The contract will define his duties, and particularly the period over which the investigation is to be made.

Upon starting his work he will require copies of the Trading and Profit and Loss Accounts and Balance Sheets for the period under review, and he will also require a list of all the books kept, and access to them when the necessity arises. If the accounts have been subjected to a professional audit he should examine the certificates or reports given by the Auditors.

The investigator will also require to know the nature of the business, and any special features relating to the book-keeping.

If the accounts have not been audited, it will be necessary for the investigator to make a sufficient examination of them to enable him to exercise his judgment in dealing with the records concerned. This will very frequently involve the equivalent to an audit.

(b) **The Preparation of Accounts on a Uniform Basis.** If accounts have been regularly prepared these should be, if necessary, re-drafted on a uniform basis so that the maximum of information can be obtained by comparison with the figures relating to each period. The best way to effect this is to have the Trading and Profit and Loss Accounts written out in columnar form, with a column for each year, leaving a special space against each column for the purpose of inserting the percentage of each item of expenditure to the turnover. The Balance Sheet should be set out in a similar manner, and from a comparison of the figures, and particularly from a comparison of the percentages, a great deal of valuable information should be obtained which will be useful in the course of the investigation.

By this means the investigator will have in a very concise form the whole of the accounts relating to the period which he is examining.

(c) **Percentages.** The use of percentages is particularly advisable in an investigation of this nature. It will generally be found that where a private business is being sold to a limited company the accounts show an increased turnover over the few years prior to the proposed transfer. In practically every case where the turnover increases, the expenses are bound to increase also, except in the case of fixed charges such as rent, rates, etc., which do not necessarily increase. Those charges which do increase, however, should not go beyond a fixed ratio to the turnover, and it would be quite reasonable to expect them to show a reduced percentage when the turnover increases. A comparison of figures only will not indicate the true relative value of the expenditure as compared with the turnover, and this can only be ascertained by taking the percentage which one figure bears to the other.

Another important piece of information which percentages give is in the case of the gross profit. If the percentage of gross profit to the turnover be compared with the same percentage for previous periods, and shows an increase, such increase must be due either to a rise in the selling price, or to a reduction in the cost of materials or labour, or to an inflation of the stock. This is a very useful and important test which is invariably utilised by accountants to determine whether the stock is valued on a proper basis. It will readily be understood by any person with a knowledge of

accounts that every penny by which the stock value is improperly inflated adds to the gross profit an additional corresponding sum, and *pro tanto* the percentage which the gross profit bears to the turnover is also increased.

To ascertain the percentage which any item of expense bears to the turnover it is necessary to multiply the figure of the particular expense by 100, and divide the result by a figure equal to the turnover. It is sufficient to treat as factors in these calculations the pounds sterling only, and the calculations should be carried to two places of decimals. Any slight differences should be adjusted to get an accurate agreement of the whole of the percentages with the turnover.

(d) **The Trading Account.** In examining the Trading Accounts it should be seen that returns are properly dealt with, and that the stocks are properly transferred from one account to the other. Percentages should also be prepared, and it should particularly be seen whether the rate of gross profit is constant, or in the alternative, the variation to which it is subjected over the period. In the case of important variation the cause in each case should be ascertained, since, as already pointed out, if it be not due to differences in the cost of materials or wages, or in the selling price, it is probably to be accounted for by errors in stock values. It should particularly be observed whether the total stock held at the end of each period tends to rise or fall in relation to the turnover.

If there is a considerable increase in the stock held without a corresponding increase of trade, this may be due to inflation of values. On the other hand it may be due to favourable markets at the time, but in any case inquiry should be made as to the reason of the increase.

The progression of the turnover is, naturally, of the utmost importance. The ratio of progression should be ascertained and any abnormal variation inquired into. It is particularly important to see that returns are properly dealt with through the whole period.

(e) **The Profit and Loss Account.** The various classes of expenditure relating to each period as shown by the Profit and Loss Account should be examined, the percentage of each to the turnover compared, and any fluctuations in such percentage inquired into. It will be remembered that with certain of these charges an increased turnover will not of necessity cause an increase of expense, so that in some cases it will often be found that the percentage of the particular expense should have been reduced. On the other hand, it is only natural to expect such items as travellers' commission to show an increased charge as against an increased turnover, but the percentage which that increased charge bears to the increased turnover should not exceed the normal percentage

of previous years. If, however, there is an increase in the percentage also, it will be necessary to ascertain the cause. Any excessive expenditure in any one year will be brought to light by means of the percentages, and the cause of it should be carefully noted.

(f) **The Balance Sheet.** By tabulating the Balance Sheets, information will be given as to the amounts annually taken credit for in respect of the various classes of fixed assets, outstanding debtors, reserves for bad debts and discounts, and expenditure paid in advance, cash balances, etc. The liabilities each year will also be compared, and any variations in the amount of working capital can easily be noted. The last Balance Sheet is very often the basis upon which the transfer will be made to the proposed company, and this should be checked in detail, and the assets verified in the usual manner. "

(g) **The Checking of Balances.** The investigator should now be in a position to decide upon the essential work to be performed in the course of his inquiry. Where the accounts have been subject to audit it will not be necessary for him to do the amount of detail checking which would be the case if the books had not been subjected to the criticism of a third party. At the same time a certain amount of work must be done, and it will usually be necessary for the investigator to check the opening balances for the period to ensure that every balance shown upon the opening Balance Sheet actually exists in the books.

It will also be necessary for him to examine the Impersonal Ledger, checking all the postings from the various books of prime entry to the nominal accounts concerned, and testing, so far as he thinks advisable, the cash postings.

The balances on the nominal accounts at the end of each year should be checked into the profit and Loss Account.

Where the books have not been subjected to audit it will not be safe for the investigator to do anything less than a complete audit. As already indicated it is considered by some accountants that where a professional investigation is made for the purpose of enabling the profits to be certified, no inquiry is necessary to see whether or not any fraud has been committed, but since a fraud, when perpetrated will, as a rule, actually affect the profits, it seems reasonable to assume that it would be expected of the professional accountant that he should allow his mind to be prepared to receive any indications of fraud which the books afford in any way, and for this purpose a complete audit is necessary.

At the same time it by no means follows that because a complete audit is desirable, every posting in the books must be checked. The common law relating to an audit will apply *mutatis mutandis* to an investigation, and the

investigator can therefore rely upon the well-known dictum—

"Where there is nothing to excite suspicion very little inquiry will be reasonably sufficient, and in practice, I believe, business men select a few cases at haphazard, see that they are right, and assume that others like them are correct also. Where suspicion is aroused, more care is obviously necessary." (Lindley L.J., in *London and General Bank*, 1895, 2 Ch. 683.)

If the turnover is to be given in detail for each year care must be taken to see that purchase returns are credited to a separate Purchase Returns Account, or are charged against the purchases. They must not be credited to the Sales Account.

(h) **Vouching.** Although the investigator should in any case check a certain amount of the detail work, and should ensure, as far as possible, that the balancing of the books is *bonâ fide*, it is not considered necessary, unless some special reason indicates that it is desirable, to vouch the cash payments even though no audit has previously been performed. The object of the investigation is to ascertain profits, and the only payments affecting the Nominal Accounts will be expenses tending to reduce profits, so that by not vouching the payments there will be no risk of an inflation of profits escaping notice.

The investigator should, however, vouch all capital expenditure to ensure that any items capitalised are not of such a nature as should have been charged to revenue. When this has been done it may be taken for granted that the remainder of the expenditure is of a revenue nature.

It is, therefore, of the utmost importance to vouch all expenditure which is charged against asset accounts in the Impersonal Ledger, and in fact to check in detail all items posted to such accounts. In doing this, care must be taken to see that such items are properly chargeable to capital, and do not represent expenditure in the shape of repairs and renewals which should have been charged against the Profit and Loss Account.

(i) **Stock Values.** The stock sheets in respect of each year should be examined and tested, and it should be ascertained whether in their preparation a proper system of check has been carried out, and whether such sheets have been duly initiated by the persons responsible for their preparation, and certified by the managing director, in the case of a company, or the proper official.

It should also be ascertained whether the basis on which the stock has been taken is uniform throughout, e.g. that stock has been valued at cost or market price whichever is lower at the date of the preparation of the stock sheets on each occasion. If stocks have been taken above cost,

or insufficient depreciation has been allowed for spoilt or obsolete stock, adjustments must be made accordingly in the years affected.

The percentage of gross profit on turnover, as already explained, should be examined; and the cause of any important variation from the normal percentage should be inquired into and satisfactorily explained.

Particular care should be paid to partly manufactured stocks. The best method of dealing with these is to take a few of such items at random and check the calculations of cost, noting whether the same appear to be reasonable.

(j) **Goods on Sale or Return.** It should be ascertained whether the sales include goods out on sale or return, in the hands of agents, or on consignment. If transactions of this nature have been improperly recorded, the necessary adjustments should be made in order to eliminate from each year's accounts the profits improperly taken in respect thereof. The result to the business is only affected by such items in the last year's accounts, but they should be adjusted in each year since it is necessary to ascertain the true profits of each year.

Any such goods having been eliminated from the sales, and a corresponding item eliminated from the debtors, can be included at cost or market price, whichever is lower, in the stock at the date of the Balance Sheet.

Care must, however, be taken to see that no goods on sale or return in the hands of the business investigated belonging to third parties are included in the stock. Strictly speaking such goods should not be taken into the accounts of the business concerned until the property in them has actually passed in accordance with Section 18 (4) of the Sale of Goods Act, 1893.

(k) **Outstanding Liabilities and Payments in Advance.** In examining the various nominal accounts care should be taken to ascertain that all outstanding liabilities at the end of each year have been taken into account; and in cases where the percentages show an undue variation, this particular point should be specially watched. At the end of the period statements from the creditors should be called for and examined against their Ledger Accounts to ensure that nothing has been omitted.

Similar notice must be taken in respect of charges which extend over more than one financial year of the business, care being taken to see that where apportionments are necessary they are made on a proper basis. The unexpired portion carried forward in the closing year can be verified by inspection of actual documents.

(l) **Bad Debts and Discounts.** The amounts charged in respect of ascertained and estimated loss on realisation of the debts and also for discounts in respect of each year should be examined

in order to ascertain whether the amount debited to Profit and Loss Account in each year has been correct. It may happen that in certain cases the reserve carried forward is larger than is actually found to be necessary during the ensuing year. No adjustment, however, will be necessary here so long as the reserve was arrived at reasonably, having regard to the information at the disposal of the business at the time it was made. In the last year, however, this question should be given more detailed consideration, the whole of the debtors' balances being checked with the schedules and examined with a view to verifying the possibility of loss in connection with them.

The usual indications of debts proving bad should be carefully looked for, and after these have been noted the debts should be gone through with a responsible official in order to ascertain that the final reserve for bad debts is sufficient.

(m) **Detailed Examination of Accounts of the last Year.** The accounts of the last year should be subjected to a detailed examination, and this is particularly necessary, even though in the judgment of the investigator a detailed examination of the previous years is not essential. This is especially the case where the final year shows an increased profit, since it is possible that, as the vendors contemplated the sale of the business during this closing year, steps have been taken to manipulate the accounts, and the increased profit is shown in consequence.

The profits of the closing year may have been increased by an inflation of the closing stock, the inclusion of fictitious sales, the omission of purchases or other outstanding liabilities, reduction in the provision for bad debts, an excessive reduction in expenses, or by paying business liabilities out of private moneys.

The closing stock should be carefully checked, and particular attention should be paid to those prices which can be checked with invoices, trade papers, etc. It should be seen that each person concerned in taking stock has initialed for the portion of the work that he has done, and a fairly exhaustive test of extensions should be made in addition to the castings.

A certain number of entries in the Day Book selected at random should be checked with the orders actually received.

Inquiry should be made into the position of affairs since the last Balance Sheet, the Returns Inwards Book being looked into carefully to see whether any excessive returns are shown therein, since these may be a consequent adjustment in respect of fictitious sales.

Any excessive reduction in expenses should be at once indicated by means of the percentages, and, if this is indicated, a detailed comparison of one year's Expenses Account with another should be made. Thus, an omission of purchases where

the goods are brought into stock should have its effect on the percentage of gross profit to turnover, and in the same way the omission of outstanding liabilities on the Expense Accounts should affect the percentages shown in respect of those accounts.

It will be difficult to bring to light a case where business expenses are paid out of private moneys, but if such has been done it will, as just indicated, have an effect on the percentages which have been prepared, and though information as to the cause may be withheld, an unexplained variation will put the investigator on his guard, and enable him to press for further information on the point in respect of which he is not satisfied.

Discreet inquiry will probably bring to light expenses of which the business had received the benefit, in respect of which no charge appears, and in the absence of a proper explanation, such charges should be treated as outstanding liabilities.

It is also desirable to compare the percentages of expenditure to turnover, not only as regards one year with another in respect of the business investigated, but to ascertain what is the normal percentage in the case of other businesses which have been examined from time to time by the investigator. This will enable the accountant to judge as to whether the expenditure is reasonable under the circumstances of the business being inquired into, and may be the means of bringing to light a consistent practice of paying business liabilities out of private moneys with a view to a subsequent flotation.

(n) **Adjustments of Profits.** The object of the investigator is to find a true figure of profit which he can certify to have been made over the period covered by his examination. In this connection it must be remembered that it is not the actual profits shown by the accounts which it is desired to ascertain, but the profits which it is anticipated will be earned by a limited company, having regard to the advantages and disadvantages which that company will possess as compared with the firm whose business is being taken over.

The following are the usual adjustments which it is necessary to take into account in this connection—

ADDITIONS TO ASCERTAINED PROFITS. (1) Interest on partners' capital and Current Accounts. These are appropriations of profit and will not arise in the case of a company.

(2) Partners' salaries, since these are really appropriations of profit and will not arise after the transfer of the business to a limited company.

(3) Income tax, since this is an appropriation of profit and would bear no relation to the charge for income tax which may have to be charged to the Profit and Loss Account of a limited company. It will be remembered that if a limited company is paying dividends, a great portion of the tax

which it pays is merely tax deducted at the source from shareholders and debenture-holders.

(4) Interest on loans and overdrafts, if any, except in those cases where the loans will be taken over by the company. If such loans are not taken over it is to be assumed that the company will be provided with sufficient working capital to enable it to carry on its business without any such loans, and such charges therefore will not be incurred by the company.

(5) The rent paid by the firm if the company is going to purchase the trade premises hitherto rented by the business.

(6) An estimated amount for discount, where, owing to lack of working capital, the business has not been able to avail itself of all discount, and it is expected that the company, by reason of a sufficient working capital, will be enabled to do so.

(7) Any exceptional losses such as those arising by reason of insufficient insurance, defalcation, costs and damages incurred by litigation, and other losses not arising in the ordinary course of business. In the case of insufficient insurance, however, although the loss can be added to the profits, a sum equal to the underpaid insurance premium should be charged against such profits.

(8) Any capital loss, such as a loss on a sale of fixed assets or loss on sale of investments.

(9) Any capital expenditure which may have been charged to revenue.

(10) Any excessive reserves for bad debts or other contingencies.

DEDUCTIONS FROM ASCERTAINED PROFITS. (1) Income from assets not taken over by the company.

(2) Rent, if no charge has been made for this in the Profit and Loss Accounts of the business, and the company is not going to buy the premises.

(3) Exceptional profits, such as compensation for compulsory removal from premises, insurance profits, speculation profits.

(4) Capital profits, such as profits on sale of fixed assets, or on investments.

(5) Sometimes directors' fees are added to the profits, but it is more usual to certify the profits without this adjustment, in which case the certificate should indicate that no charge has been made for this expense.

Depreciation will also require to be adjusted, if possible, to the true measure of depreciation which the company will have to charge to make good expired capital values, but as will be shown this is very often found impossible to adjust, and a certificate is therefore given accordingly. It will be seen that if the profits are adjusted by such items as those indicated, the resulting net profits will approximate those which may be legitimately anticipated from the carrying on of business by the company.

(o) **Depreciation.** If the actual amount of depreciation which the company will require to

make good in each year could be properly ascertained, an adjustment thereof could be made on the actual profits shown by the accounts, but usually it is found impossible to ascertain this depreciation with any degree of certainty, and therefore the depreciation which has been charged is added to the profits and a certificate given accordingly.

The reason for this is the fact that the fixed assets which the company will work may differ very materially from those which have been employed in the business before it was taken over, while even if the same assets are to be used, the basis of valuation would probably differ to such an extent as to render the charge for depreciation misleading if it were included as shown in the accounts. Moreover, the company may depreciate its assets, quite apart from values, on a different basis from that which has been utilised by the business formerly; and it is well known that under the various methods of depreciation the charge against profits may vary very considerably in respect of assets having the same life period. If a proper charge can be calculated, it would be desirable, of course, to include it; but a calculation of depreciation depends on the state and age of the assets, on the estimated life, on the value placed upon the assets, and upon the basis of depreciation employed. In consequence of these important points it is usually considered better to leave depreciation out altogether and to certify a higher profit, making it quite clear in the certificate given that depreciation has been ignored.

(p) **The Separation of each Year's Profits.** It is very important to set out each year's adjusted profits separately in the certificate given. If the investigation had extended, for instance, over five years, to take the average of those profits and to certify one figure, would be unfair and misleading. If the profits have fluctuated considerably, and there has possibly been a loss in one or more of the years taken, it would leave the intending shareholder entirely in the dark as to the true state of affairs over the period investigated; and if the profits have shown a genuine and healthy progression, it would be unfair to the promoters as well as misleading to the intending shareholders.

As the status of the professional accountant has increased in value in the eyes of the public, it is essential that no member of the profession should give his information in a manner prejudicial to the public, merely for the purpose of obliging the company promoter. Every professional accountant should, therefore, aim at giving his opinion in the fairest possible manner so that no member of the public may be misled by the form of the information which he gives.

(q) **Certificate.** The certificate given as the

result of investigation should be worded clearly and without ambiguity. It should state the period covered by the investigation, and should set out the profits of each year of the period separately. The turnover of each year may be given if desired. The certificate should state that the necessary adjustments have been made, and in the case of special adjustments, should definitely state what has been done; while if any expenses are not taken into account in arriving at the certified profits, a note should be made as to these, e.g. depreciation, as already mentioned.

The certificate should deal with facts, and estimates or opinions should not be given since it might be supposed that such estimates or opinions were actual facts elicited from the books, and this would create a wrong impression. It is very undesirable that the accountant giving the certificate should indicate that any particular set of charges will be covered by the profits, nor should he, whatever his knowledge may be of the particular class of business, express any opinion as to the possibilities of the actual business to which the certificate relates.

The certificate should be such that an ordinary intelligent person, whether a business man or not, can therefrom assess for himself the possibilities of the new company. It should be framed with the utmost care and caution, since this is the only object which it is required to serve.

The following is a good example of a certificate as given by a leading firm of chartered accountants.

"We have examined the books of John Jones & Sons, Ltd., for the three years ending 31st December, 1921, and find that after making the proper adjustments, but before charging Depreciation on Buildings, Plant, Machinery and Tools, the Profits are as follows—

1919	..	..	£29,508	6	11
1920	..	..	27,524	5	9
1921	..	..	30,962	7	4

*Signed
Chartered Accountants."*

Where a limited company is formed to take over a business which has been built up within a comparatively short space of time by means of an extensive advertising campaign, it is quite possible that the normal advertising necessary to maintain the turnover so created cannot be estimated. If no advertising is charged in arriving at the certified profits, it is essential that the certificate should not only clearly indicate that this is the case, but it is submitted that such certificate should state the actual cost of the advertising which has been utilised in creating the business.

(r) **Illustration of Accounts with Adjustments and Certificate.** The following are the accounts

TRADING AND PROFIT AND LOSS ACCOUNT
FOR THE THREE YEARS ENDING 31ST DECEMBER, 1921.

	1919		1920		1921		%		1919		%		1920		%		1921		%		1921	
	£	s. d.	£	s. d.	£	s. d.			£	s. d.			£	s. d.			£	s. d.			£	s. d.
Jan. 1 To Stock	15'86	2,030 10 5	16'81	2,354 8 0	17'97	2,840 10 11			100'00	12,863 8 0	100'00	14,007 8 6	100'00	15,803 1 7								
Dec. 31 " Purchases	56'92	7,286 18 0	55'78	7,813 3 3	47'93	7,570 8 6				2,354 8 0		2,840 10 11		3,923 6 5								
" " Wages	7'09	907 18 6	8'23	1,153 4 6	7'75	1,224 3 3				2,354 8 0		2,840 10 11		3,923 6 5								
" " Balance being																						
" " Gross Profit	38'52	4,932 2 8	39'46	5,527 3 8	51'21	8,091 5 4																
	118'39	15,157 9 7	120'28	16,847 19 5	124'83	19,726 8 0			118'39	15,157 9 7	120'28	16,847 19 5	124'83	19,726 8 0								
To Trade Expenses	2'78	356 7 5	2'79	390 7 10	3'20	506 3 2																
" " Advertising	1'37	175 4 6	1'61	225 3 0	'95	150 7 4																
" " Salaries	3'48	445 10 0	3'46	485 5 6	3'29	520 10 0																
" " Commission	3'21	410 7 3	2'79	390 3 4	2'91	460 3 6																
" " Travelling Expenses	6'51	833 10 4	5'51	772 8 6	7'00	1,106 8 3																
" " Rates and Taxes	1'66	212 5 3	1'40	196 2 0	1'22	193 4 6																
" " Office Expenses	2'39	306 8 4	2'39	335 7 3	2'20	347 10 5																
" " Bad Debts	'60	76 5 7	'78	109 6 0	'54	84 12 0																
" " Discount on	1'18	151 7 9	1'24	173 2 4	1'15	182 7 4																
" " Depreciation on	'09	12 0 0	'09	12 0 0	'08	12 0 0																
" " Furniture																						
" " Plant and Machinery																						
" " Repairs and Renewals	'66	84 6 10	'65	90 10 0	'66	103 6 8																
" " Accountant's Charges	'96	123 2 9	1'04	146 3 7	'86	135 8 10																
" " Interest on Loan	'25	31 10 0	'22	31 10 0	'20	31 10 0																
" " Income Tax	'39	50 0 0	'36	50 0 0	'32	50 0 0																
" " Interest on Capital	'67	85 6 0	'44	62 8 6	'56	89 11 1																
" " Balance being	1'95	250 0 0	1'78	250 0 0	1'58	250 0 0																
" " Net Profit	16'31	2,088 10 8	16'47	2,307 5 10	24'49	3,868 2 3																
	44'46	5,692 2 8	43'02	6,027 3 8	51'21	8,091 5 4			44'46	5,692 2 8	43'02	6,027 3 8	51'21	8,091 5 4								

of the business of R. Thompson & Co., for the years 1919, 1920, and 1921, set out on a uniform basis with the percentage of each item of expense in relation to the turnover.

The following errors in the year 1921 are found in the course of the investigation—

£750 purchases at the close of the year have not been passed through the Invoice Book or treated as outstanding but are included in the stock.

There are errors in the extension of the stock sheets reducing the value of the stock by £518 4s. 2d.

The stock sheets are overcast by £500 1s. 0d.

It was found that £75 due on Advertising Account was omitted from the accounts.

R. Thompson & Co. have their own premises and a large piece of real estate adjacent thereto. The company is not taking over the property but has agreed to pay a rent of £180 per annum for the business premises.

INVESTIGATION ON BEHALF OF A PRIVATE INDIVIDUAL OR FIRM ABOUT TO PURCHASE A BUSINESS.—(a) Preliminary Considerations.

Where a business is to be entirely purchased, the investigation will resolve itself into an inquiry as to the profits which have been made in the past with a view to putting a definite value upon the goodwill of the business. The purchase price of the business will depend to a certain extent upon the assets taken over, and also whether the liabilities will be discharged by the vendor or by the purchaser. The amount of the assets and liabilities can be ascertained, but where a sum is paid for goodwill it will be based on the profits of the past, and it is necessary to ascertain these as exactly as possible.

Goodwill may be defined as the value attaching to the reputation of a business and to the likelihood that custom will continue to be attracted in the future as in the past, notwithstanding the

ADJUSTMENT ACCOUNT

	1919			1920			1921				1919			1920			1921		
	£	s.	d.	£	s.	d.	£	s.	d.		£	s.	d.	£	s.	d.	£	s.	d.
To Profit on Sale of Land	760	0	0	500	0	0				By Net Profit	2,088	10	8	2,307	5	10	3,868	2	3
„ Rent of Business Premises	180	0	0	180	0	0	180	0	0	„ Depreciation of Furniture	12	0	0	12	0	0	12	0	0
„ Purchases Omitted							750	0	0	„ Depreciation of Plant and Machinery	84	6	10	90	10	0	103	6	8
„ Errors in Stock Extensions							518	4	2	„ Interest on Loan	50	0	0	50	0	0	50	0	0
„ Stock Overcast							500	1	0	„ Income Tax	85	6	0	62	8	6	89	11	1
„ Advertising omitted							75	0	0	„ Interest on Capital	250	0	0	250	0	0	250	0	0
„ Net Profits of Company	1,630	3	6	2,092	4	4	2,349	14	10										
	£ 2,570	3	6	£ 2,772	4	4	£ 4,373	0	0		£ 2,570	3	6	£ 2,772	4	4	£ 4,373	0	0

NOTE.—The Stock errors reduce the gross profit for 1921 to £6,323 os. 2d., which equals 40·01 per cent. on Turnover, which is a reasonable figure in the absence of any other factors causing fluctuations from the normal.

The following certificate will show the profits which can be certified in the company's prospectus.

"We have examined the books of R. Thompson & Co. for the three years ending 31st December, 1921, and find that after making the proper adjustments, but before charging Depreciation on Plant, Machinery and Furniture, the Profits are as follows—

1919	..	..	£1,630	3	6
1920	..	..	2,092	4	4
1921	..	..	2,349	14	10

Signed. X Y & Co.

Chartered Accountants.

London, E.C.2

Date....."

change of proprietorship. It may originate in one of three ways or a combination of them—

(1) By means of the reputation of the article produced as apart from the personality of the proprietors.

(2) By means of the business possessing special advantages in the shape of local or partial monopoly, patents, trade-marks, situation of premises, etc.

(3) By the personal reputation and influence of the proprietors.

The value of goodwill is usually based on the average profits for a term of years, but in many cases, e.g. retail shops, it is based on the turnover.

(b) **Nature and Locality of Business.** It is essential that the investigator should make himself thoroughly acquainted with the nature of the business; not only generally but particularly. Thus, if the business be that of a draper, who

has dealt mainly with certain lines, this fact is of the utmost importance since it is to be assumed that the customers in respect of whom the goodwill exists will only be attracted in the future for the same reason as they have been attracted in the past, *i.e.* the reputation which the business has acquired in respect of goods of that particular line.

The locality of the business is also a point to be noted, since every locality has a varying value from a selling point of view in respect of particular classes of business. Moreover, although it is to be assumed that the purchaser is aware of facts relating to the locality, it may, nevertheless, be desirable to bring to his notice any detrimental points which may be ascertained as to the locality. The street in which the business is carried on may be losing its reputation as a business thoroughfare, the neighbourhood may be socially deteriorating, etc.

(c) **The Reason for Vendor Selling.** It is important to inquire carefully as to the reasons which cause the vendor to part with the business. It is not suggested that the investigator should confine his questions on this point to the vendor, but he should, in addition, address diplomatic questions on this point to other persons connected with the business with whom he may come in contact. The value of the business would naturally not be affected if it were an actual fact that the vendor was retiring on account of age, or that he had built up a fortune, or that his health necessitated retirement; but the vendor is very apt to mention, in a casual off-hand manner, such a reason as one of these without expressly stating that such is the actual case, and so mislead the purchaser into making a false conclusion.

The investigator should therefore be careful to inquire of the vendor and other persons as indicated, so that he can afford the purchaser the fullest possible information on this important matter.

(d) **Powers of the Investigator.** The investigator is assumed to be the agent of the purchaser, and in order that he may examine into everything of importance, it is essential that he should be armed with all particulars of the proposed agreement, and empowered to demand all the information which he considers necessary.

He will therefore want to know what assets are being acquired, and the values placed upon them; what liabilities are being taken over; on what basis the goodwill is to be determined, or if a price be already fixed in respect thereof, what that price is; whether any part of the business is not being transferred by the vendor, and whether the vendor is still continuing business. If the vendor be still remaining in business, it is important to ascertain whether there is any restraint on the area in which he can carry on business; and

whether the vendor retains any rights with regard to soliciting his old customers.

The investigator would also require full power to demand information as to the basis of valuation of any of the assets or liabilities; also to have the fullest access to the books and any vouchers or other documents supporting entries made therein. Copies of any accounts which have been prepared and which form the basis of the negotiations must also be at his disposal.

Where the goodwill is based on the turnover the utmost precautions should be taken in verifying the sales. Where the goodwill is based on the net profits, accounts should be prepared in the form already indicated, and profits should be prepared in the same manner so that the utmost possible information can be obtained from a comparison of the accounts.

All the precautions mentioned will apply *mutatis mutandis*, but the only adjustments necessary, as a rule, will be in regard to income from assets not taken over, exceptional profits, depreciation, and exceptional losses. A proper depreciation charge must in this case be fixed, and cannot be neglected in determining the goodwill value.

(e) **Verification of Assets.** Where the purchase agreement does not provide for a separate valuation of assets, it is desirable that the investigator should verify the existence of the assets as far as possible. He should also inquire into the rates of depreciation which have been provided for during the period over which his investigation extends, and compare these with the ascertained life of the asset, to see whether it be adequate. Where it appears that the assets stand in the books at a higher figure than their true value to the business as a going concern, this matter should be pointed out to the purchaser.

(f) **The Investigator's Report.** The investigator should report fully on the whole matter to his client. His report should state the period covered by the investigation, and all salient information which he has acquired in the course thereof.

INVESTIGATION ON BEHALF OF A PERSON WHO IS PROPOSING TO TAKE A PARTNERSHIP IN A GOING CONCERN.—(a) **Preliminary Considerations.** In the case of an investigation into accounts where an individual is acquiring a share in an existing partnership, the preliminary considerations will, *mutatis mutandis*, be similar to those in the case of a person buying the whole business. There is, however, as a rule, this difference, that where a man buys a business he is generally fully acquainted with the technical nature thereof, whereas it frequently happens that a man acquires a partnership with no knowledge whatever of a business of that nature.

It is therefore very important that the investigator should inquire not only into the profits that

have been made with a view to determining the value of the share of goodwill, and into the values at which the assets stand in the books, but also into the nature and character of the business carried on. He should also inquire into the technical points necessary for its proper conduct, so that he may advise his client in such a way that he is aware of any difficulties that may present themselves to the proprietors of the business, and of any facts which might act as a deterrent to his acquiring a share of a business with which he would not really like to be associated.

It must be remembered that where one partner has all the technical knowledge, a partner not possessing that knowledge is at a great disadvantage as a proprietor of the business, since he is to a very large extent in the hands of the man who possesses the necessary knowledge. This latter individual may or may not be a desirable partner, and if inquiries indicate that he is not, he is still more undesirable if the control of the business must be entirely in his hands.

Again, the business may be of such a character that a man with the ordinary standard of self-respect would not care to be associated with it if he knew its real character, as, for instance, a business for the manufacture of imitation antiques where most of the clients happen to be antique dealers. This is a question of ethics, but it is advisable that any such point should be brought to the notice of the client for whom the investigation is being made, not with the idea of prejudicing him, but with a view to placing the fullest possible information before him so that he can exercise his judgment.

The locality of the business is also important for reasons that have been indicated in the previous section, and another point of the greatest moment is the reason why an additional partner is required.

If a new partner be required to take up the share of an outgoing partner, it is very important to ascertain the value of that outgoing partner to the business. The business may suffer very considerably by losing the services of the outgoing partner, and his value may not be compensated for by the technical knowledge of the incoming partner or the remaining partners, so that the value of the share of goodwill must be considered from the point of view of the fact that the services of the retiring partner will not be available.

Where the incoming partner does not possess the necessary technical knowledge it is perfectly clear that it is his money which is required, either for the purpose of paying out the retiring partner, the new partner taking up his share, or to provide additional capital for the business. If additional capital be required, the investigation must be directed primarily to ascertaining the reason why

such capital is wanted. It may be due to the fact that the expansion of business necessitates further capital being introduced, but on the other hand it may be due to the fact that the existing partners have been improvident in their conduct of the business, and that they have drawn out more money than the business could reasonably be expected to provide.

(b) **Powers of an Investigator.** The investigator should be placed in possession of all material facts which the client has received, and he should take every precaution to verify these by inquiry, not only from the principals of the business whose accounts he is investigating, but also from persons employed therein, and from any other sources that may be available. He should be empowered to demand all necessary information in order that nothing may be concealed from him which might influence his judgment if he knew of it. Cases have been known where accountants have investigated books, and certain information has been withheld from them, the principals of the business considering the information as private, but agreeing to disclose the facts to the client of the investigator. Such a course should not be agreed to by the accountant making the investigation, and he should advise his client in such a case that unless the facts required are disclosed to the person entrusted with the investigation, negotiations should be broken off; the point being that however satisfactory it might appear to the client, it would by no means follow that the account given of the particular points would be satisfactory to a person skilled in investigating such matters.

(c) **Scope of Examination.** The points dealt with in the previous sections will apply, *mutatis mutandis*, in the present instance, the principal objects being—

(1) To verify the Balance Sheet and the Profit and Loss Account which are put forward as the basis of negotiations.

(2) To ascertain the probable amount of profit that would be attributable to the share of the incoming partner.

(3) To ascertain whether the value to be given for the share of goodwill by the incoming partner is reasonable.

(4) To determine whether or not the capital (if any) to be introduced by the incoming partner is reasonable.

A careful examination should be made to ensure that all outstanding liabilities are brought into account, particularly with regard to estimated liabilities, such as freight on foreign sales made C.I.F., foreign duties payable by the seller, and contingent liabilities.

It is also important to see what forward contracts have been entered into, since it may be found that sales for future delivery have to be bought in on a rising market, or that purchases

for future delivery have to be taken in on a falling market.

(d) **The Investigator's Report.** The report to the client must include all information coming to the knowledge of the person making the investigation, which will enable the client to arrive at a decision as to whether the proposed partnership should be entered into.

It should advise the client on any point where it may be considered that the terms of the partnership are not reasonable, and should give any information which may be ascertained as to the cause of the new partner being required. Any indication of financial difficulties involving one or more of the existing partners should also be reported.

If it be found that the values placed upon the partnership assets are inflated, the client should be informed of this since the capitals of existing partners will also be inflated, and this would prejudicially affect the incoming partner both as to the interest taken by other parties and in the value of his share in the event of a dissolution.

(e) **The Partnership Agreement.** It is very desirable in such cases that the investigating accountant should also advise as to the financial clauses in the partnership agreement where the partnership is actually entered into.

This is not only for the purpose of safeguarding the rights of the incoming partner while the business is a going concern, but also to ensure a satisfactory method of ascertaining his share if he retire, or of determining his rights in the case of dissolution.

The usual financial clauses of a partnership deed are as follows—

(1) As to capital, and whether each partner should contribute a fixed amount or otherwise.

(2) As to the division of profits and losses between the partners, including capital profits and losses.

(3) Whether the capitals are to be fixed, drawings and profits being adjusted in Current Accounts, or whether the same are to be adjusted in the Capital Accounts.

(4) Whether interest on capital or drawings, or both, should be charged, and the rate thereof.

(5) Whether Current Accounts (if any) are to bear interest, and the rate thereof.

(6) Whether the drawings in advance of profits are to be limited.

(7) As to the partners' salaries (if any).

(8) That proper accounts shall be drawn out at least once a year (all assets of a fluctuating nature being brought in at a valuation), and that the same shall be audited by a professional accountant, and signed by all the partners.

(9) That such accounts shall be binding on the partners, but can be re-opened in the case of manifest error within a specified period.

(10) That the method of determining the amount of goodwill in the event of the retirement or death of any one of the partners shall be fixed.

(11) That in the event of the death of a partner the method of determining his capital shall be stated, whether he is to be entitled to his capital as per the last Balance Sheet, plus interest at a certain rate per cent. in lieu of profits, or whether accounts are to be taken at the date of death, and his share of profits up to that date credited, and whether or not the assets of the partnership are to be subject to re-valuation.

(12) That in the event of partnership insurance policies existing, the method of treating the premiums and the division of the policy money shall be determined.

This, of course, forms no part of the actual investigation, but it follows that the person who has made the investigation is in the best position to safeguard his client against any points which might otherwise prejudice him, which he has come across in the course of the investigation.

INVESTIGATION ON BEHALF OF INDIVIDUAL OR FIRM PROPOSING TO FINANCE A BUSINESS BY ADVANCING MONEY TO THE PROPRIETORS OR TAKING UP SHARES OR DEBENTURES IN A PRIVATE COMPANY.—

(a) **Preliminary Considerations.** Preliminary considerations in an investigation of this nature will involve inquiry into the nature and locality of the business, and particularly into the character and ability of the persons who have the control and conduct of it. The issue is clearly defined in such a case, since the whole object of the proposed agreement is to provide funds for the carrying on of the business, but however stringently the agreement may be drawn, it must not be overlooked that the control of the funds which would be provided by the client of the person making the investigation will be entirely in the hands of those who have the control and conduct of the business. The fullest possible information should therefore be first obtained as to the nature of the business and the scope of its operations, the locality in which it is carried on, and the technical knowledge and experience of the proprietors or directors, together with any information as to their antecedents which can be acquired.

(b) **Scope of the Investigation.** So far as the accounts are concerned the investigation should aim at three things—

(1) The earning capacity of the business.

(2) The ascertainment of the true position of affairs at the date of the investigation.

(3) The causes which have operated to produce the shortage of capital by reason of which further money is required.

So far as the ascertainment of profits is concerned the work incidental thereto will be carried out on lines which have already been indicated,

the progress of the turnover, the rise or fall in profits, and variations of expenditure, being carefully inquired into and tabulated.

In ascertaining the present position of affairs, the book value of the assets must be subjected to scrutiny with a view to ensuring that adequate depreciation has been written off during the time that the assets have been held. It also must not be overlooked that this may have a direct bearing on the results shown by the business in the years covered by the investigation.

The necessity for additional working capital will be ascertained, partly by the results shown in the books, and partly by inquiry. It may be due to the expansion of business which would be demonstrated by the increasing turnover, and a consequent increased amount of capital locked up in assets such as stock and book debts. Again, it may be due to the fact that the business has lost the advantage of certain capital which it has enjoyed in the past, *e.g.* through the death of a partner and the consequent necessity to pay out his share of the business to his legal personal representatives, or to the paying off by agreement of existing debentures or loans. The shortage of capital may, however, be caused by excessive drawings of the proprietors, or large sums drawn in advance of profits by directors, or by dividends being paid before profits are actually earned, or similar circumstances indicating a lack of prudence on the part of those responsible for carrying on the business.

Cases where the business may have sustained heavy loss in the past, and yet have good possibilities before it if funds are available to keep it going constantly occur, and in such cases it will be necessary to inquire carefully into the cause of such losses, which may or may not be the ordinary misfortunes to which every business is liable at times. There is also the possibility of entirely new business being entered into if sufficient capital is forthcoming to enable it to be done. In all these cases it will be necessary to examine carefully the estimates upon which future results are anticipated, to ensure that there is a reasonable probability of the capital being employed usefully if it is advanced.

(c) **Nature of Security for Advance.** A most important factor in a proposed financing of a business is the security which is offered. In the case of the proprietor being a sole trader or a firm of partners, it must not be overlooked that if a rate of interest varying with the profits is taken, it requires a very carefully drawn agreement to ensure that the person lending the money shall not be liable as a partner, with the possibility of such person being a deferred creditor in the event of the insolvency of the business.

It is therefore essential to take into consideration whether or not collateral security should be

obtained in consideration of the proposed advance, and the nature and value of that which may be offered should be subjected to close scrutiny.

In the case of a company the security will generally take the form of debentures, and inquiry should therefore be made as to any existing mortgages or charges which might have priority over that given for the present advance.

Reference should be made to the Register of Mortgages and Charges, in which all such securities will be recorded. In the case of a floating charge the directors may have power to create mortgages or charges in priority to the debentures secured by the floating charge, but if the directors are debarred from creating prior mortgages or charges and the person to whom a purported prior charge knew of such restriction, he cannot obtain priority.

Priority cannot be obtained over the debenture holders secured by a fixed charge unless the title deeds have been left in the possession of the directors, when they might raise money on them by a deposit, or by way of an equitable mortgage in which case the person advancing money is not bound to inquire as to the existence of the debentures, and having taken the securities without notice of prior charge, will have priority over the debenture holders.

If debentures are issued at a discount in consideration of the advance, the provisions of Section 212 of the Companies (Consolidation) Act, 1908, must be borne in mind. This section provides that where a company is being wound up a floating charge on the undertaking or property of the company, created within three months of the commencement of the winding up, unless it is proved that the company immediately after the creation of the charge was solvent, is invalid except for the amount of any cash paid to the company at the time of, or subsequent to the creation of, and in consideration for the charge, together with interest on that amount at the rate of 5 per cent. per annum.

The importance of registration of debentures and mortgages at Somerset House must also be remembered. Unless these are registered within twenty-one days of creation they will be void against the liquidator or any creditor of the company.

(d) **Investigator's Report.** The report should deal with every matter coming to the notice of the person making the investigation which is likely in any way to influence the judgment of the person proposing to advance money. It should set out the period covered by the investigation, the actual facts ascertained as regards profits, values, the causes necessitating the introduction of further money, and the proposed security; and should give such advice as may be called for either

expressly or by implication, having regard to the result of the investigation.

INVESTIGATION ON BEHALF OF A SHAREHOLDERS' COMMITTEE.—(a) **Powers of the Committee.** It is by no means an unusual thing for a meeting of shareholders of a company to appoint a committee to investigate the company's affairs, and when this is the case it frequently happens that the members of the committee so appointed require the assistance of an expert in such matters to enable them to bring to a successful conclusion the duty which has been imposed upon them by their fellow shareholders.

The investigator should examine the resolution of the shareholders in order that he may see the precise terms in the resolution under which the committee is appointed, and having ascertained as much as possible of the general position of the company's affairs, and the causes which have given rise to the appointment of the committee, he will be in a position to appreciate more fully the object of the investigation. His own mandate will come from the committee, but it is advisable to get it agreed in the light of full knowledge of the circumstances existing prior to the execution of any work.

(b) **Scope of the Investigation.** The scope of the investigation will depend to a very large extent on the terms of the resolution under which the committee is appointed, and the requirements of the committee so far as the investigation is concerned. It is probable that it will extend considerably beyond the accounts merely, since it is generally found that it is the management of the business which is subject to criticism.

The accounts being a record of past facts, these facts will be largely determined by the management of the business; but the investigation will go beyond the accounts in this sense, that it should have for its aim the discovery of the actual causes which have brought about the position of affairs necessitating the investigation. A large portion of the inquiry into the management will probably be made by the committee itself, but so far as the accounts and all matters affecting them, such as the counting-house arrangements, internal check, costing, and the financial policy, etc., are concerned, there will be ample material upon which the investigator can bring his professional skill to bear.

What has been already stated with regard to the critical examination of the past accounts relating to the period of the investigation will apply with the necessary modifications in this case.

If the circumstances warrant it the possibility of fraud must be assumed so that no suspicious circumstances are overlooked.

(c) **The Report of the Investigator.** The report will be made to the committee by which the

investigator is employed, and should aim at placing before it the facts ascertained during the investigation, so that the members can form their own conclusions as to what shall be disclosed to the shareholders, or as to what shall be done having regard to the powers conferred upon them.

INVESTIGATION ON BEHALF OF THE PROPRIETORS OF A BUSINESS INTO A KNOWN OR SUSPECTED FRAUD.—(a) **Preliminary Considerations.** Where fraud is merely suspected, the accountant making the investigation must get into touch with the whole circumstances of the business concerned. He will require to know the nature of the suspected fraud, and who is suspected of perpetrating it, and the reasons which are held to justify the suspicion. It is desirable that he should obtain full explanation of the system of internal check in operation, the names and duties of all members of the staff, and a complete list of the books in use.

The scope of the investigation will depend largely on the particular circumstances of the case, and the investigator must bring all his faculties to bear upon the position before deciding the work he will perform, and the course of procedure which he will adopt.

In the case of a suspected or known fraud in relation to goods only, it will also depend upon the circumstances, and particularly upon the internal check as regards goods, what course will be adopted, and it is perhaps better, therefore, to take the case of an accomplished fraud in relation to cash where the defaulting party is known and where the object of the investigation is to discover the extent of the fraud.

(b) **Internal Check.** The question of the system of internal check is of the utmost importance. Internal check is a system adopted in a counting-house whereby every transaction which is recorded in the books is subjected to a check by a person other than the man who made the record, so that there are at least two persons responsible therefor.

It is unnecessary here to outline a complete system of internal check, but it may be mentioned that every system should provide for a well defined method of dealing with cash receipts and payments, and should separate the work of the cashier from that of the ordinary book-keepers so that the cashier is not in a position to cover up any fraud which he may perpetrate by fictitious entries in either the books of prime entry or in the ledgers. It will therefore be seen how important it is for the person making the investigation to master the system of internal check so that he may know what possibilities the defaulter had to perpetrate fraud, and so that he may bring the greatest vigilance to bear upon the weak parts of the system.

(c) **Cash Frauds.** Assuming therefore that the investigation refers to a known fraud in relation

to cash, the defaulting party being known, the following are the principal points of the investigation—

(1) **THE CASH BOOK.** The Cash Book should be cast and vouched in detail. Where counterfoil receipt books have been utilised, the counterfoils should be checked against the receipts, and if any further evidence be required this should be called for. Special care should be taken in examining vouchers for payments to note any that appear to be irregular, and it is advisable that all returned cheques and discounts thereon should be examined. In the case of vouchers being missing, duplicates should be obtained; and all amounts charged to the Drawing Accounts of the partners should be initiated by them as being correct.

The appearance of the voucher itself is of the utmost importance, cases having been known where a fraudulent cashier has had invoices and receipt forms specially printed to assist him in the purported verification of bogus payments.

In examining the vouchers the particular points to note are the date, the nature of the payment, the name of the person signing the receipt, the name of the person to whom the receipt is made out, whether a stamp is affixed where necessary, and, if invoices are filed with the receipts, that proper invoices are attached to support the payment. Where postings are made to a nominal account direct the invoices should always be attached to the receipt.

Points to be noted as regards invoices are shown below.

The Pass Books should be checked completely with the Cash Book, particular attention being paid to the dates when the receipts are paid in and to ascertaining that each day's receipts have been included.

Where moneys received from debtors have been misappropriated it is common to find that in order to prevent the debtor's account appearing overdue in the Sales Ledger, moneys received from subsequent debtors are placed to the credit of the debtor whose remittance was originally misappropriated, this process being continued indefinitely. In such cases it may become necessary for the cashier to divide certain cheques in order to obtain the exact amounts necessary for his purpose, and one method of discovering whether this has been done is to obtain, if possible, the original paying-in slips from the bank and to compare them with the counterfoils of the Paying-in Book. The slip presented to the bank will contain a correct record of the amount of each cheque, whereas the counterfoil will show any improper division that may have taken place. This also serves as a check upon the improper manipulation of discounts by the same method.

All discounts of any consequence appearing in the Cash Book should be tested with a view to

ascertaining if they are in order, any doubtful cases being specially inquired into. It will be necessary to ascertain the terms of credit which may vary as regards different parts of the business.

A reconciliation statement should be prepared, or if one exists it should be checked, to ensure the agreement of the Pass Book with the Cash Book, and certificates of the bank balances at beginning and end of the period should also be obtained.

(2) **WAGES.** Particular attention should be paid to the wages sheets, in connection with which many frauds are perpetrated, often in small weekly amounts rendering detection very difficult. A great deal will depend here upon the system of internal check in operation, and it is essential that to prevent collusion at least two persons should have been concerned in every portion of the preparation of the wages sheets. If proper time records are kept, *e.g.* an automatic clock and a foreman's record, these can be checked one against the other, and also against the wages sheets themselves; and it may be possible to check the total number of hours worked against the time records, thus avoiding the necessity of completely checking all the sheets in detail. It is desirable to check one or two weeks, however, and exhaustively inquire into them, and in any cases where the necessary signatures of parties concerned in the preparation of the sheets are not appended, the examination of such sheets should be of a searching character.

(3) **THE PETTY CASH BOOK.** The Petty Cash Book should be vouched and cast. As this is a likely source of fraud, special attention should be paid to the system which is adopted since this will indicate possibilities of peculation which the petty cashier may have.

Where the imprest system is adopted and the petty cashier's account is properly checked before his expenditure is reimbursed to him, there is less likelihood of fraud being perpetrated than where round sums are given as required without past expenditure being inquired into.

Vouchers ought to be obtained for all payments of petty cash, and if this be made a rule everybody concerned will soon get into the way of handing a slip to the petty cashier when money is taken. If this be not done it will be very difficult to ensure the *bonâ fides* of numerous small items.

(4) **INVOICES.** Invoices should be vouched with the Bought Journal, and while this is being done, a sharp look out should be kept for duplicates. If a duplicate invoice gets entered into the Bought Journal two credits will be made in the account of the person supplying the goods, and two cheques could be drawn against these two credits, one being sent to the party entitled to it and the other being fraudulently misappropriated.

In order to ensure that all the invoices represent *bonâ fide* payments, it should be seen that they

have been properly checked. The points to be noted as regards this are as follows—

(1) A reference to the Goods Invoice Book should be shown on the invoice. At the time this reference is put on, the entry in the Goods Inwards Book should be so marked that it cannot be utilised for second invoices.

(2) The number of the counterfoil in the Order Book should be shown thereon.

(3) The initials of the invoice clerk should appear indicating that all calculations on the invoice have been checked.

(4) The initials of the buyer should be given to show that the price is correct.

(5) The initials of the departmental manager or his authorised deputy should be shown to ensure that the invoice is approved as a whole.

(6) If invoices are attached to the cash vouchers, the statements should also be attached, and the totals of the invoices should be checked thereon.

(7) Any deductions by way of trade discount should be agreed; and any deductions by way of contra accounts should be noted on the statement.

(5) **ALLOWANCES, RETURNS AND BAD DEBTS.** All allowances and bad debts shown in the Credit Book and the Journal should be inquired into since it is possible that there may be an attempt to conceal misappropriations of money by passing a credit to the customer's account through these books. It is therefore necessary to vouch all such items. In the case of returns the receipt of the actual goods returned should be traced.

(6) **CASH SALES.** Where there are a large number of cash sales it is necessary to examine the system adopted for dealing with these. The proper method is to separate the selling department from the cash desk, the salesman making a duplicate invoice for each sale, the copy of which will act as a check against the amounts received by the cashier. If such a system be not in force, it will be very difficult to trace defalcations, but if it be found that the receipts from cash sales have declined, whether as a whole, or so far as one particular salesman is concerned, the fullest inquiries should be made.

(7) **THE VERIFICATION OF LEDGER BALANCES.** The best method of verifying the balances on the Sales Ledgers, where it is suspected that amounts have been misappropriated, is for the accountant to obtain instructions to send out a circular to the debtors, stating the amount of the balance as shown in the books, and asking for communication to be made to him in the event of the figure not being correct. It frequently happens, however, the proprietors of the business do not care for this to be done, and in any case, their permission must be obtained in the first instance. Where such circularisation is not carried out, it will be

impossible for the accountant to make sure that he has traced the whole of the misappropriations from this source, although these will declare themselves in due course, as statements are sent out.

Where the defaulting party has had access to all the books, it will be necessary for the whole of the postings to be checked, and the books cast, and a trial balance obtained. In checking the Sales Ledgers, special attention should be paid to allowances, returns and bad debts written off, for reasons already indicated. In some cases it may be found that the defaulting party has omitted to record sales in the Sales Day Books, in order that when remittances are received he can appropriate the same without having to falsify the books further. In order to ascertain whether this has been done, the Order Book should be tested with the Sales Day Books, to see that all orders that have been executed have been entered up, and, if necessary, reference should be made to the Goods Issued Book.

(8) **BILLS OF EXCHANGE.** All bill transactions should be checked and the proceeds of bills matured accounted for; and in the case of dishonoured bills it should be seen that these are charged back to the person responsible to the business for the payment thereof.

Bills of Exchange on hand or with bankers for collection should be examined or certified.

(d) **Compensating Adjustments to Conceal Fraud.** It is true that the perpetration of fraud is more difficult to conceal where books are kept by double entry than would be the case where a single entry system is in operation, but with a skilful book-keeper who has access to all the books, it is quite possible that a fraud can be perpetrated and a compensating adjustment made in the books so that the double entry is not affected.

To give one illustration of this, it may be assumed that the cashier receiving £50 in cash from a customer, X, enters £25 in the Cash Book and puts the remaining £25 in his pocket. He then credits X's Account by Cash £50, and in the usual manner adopted in the counting-house ticks off the £25 debit in the Cash Book against the £50 credit in the Ledger. The result of this one transaction would be that the books of the firm would contain an excessive credit to the extent of £25. To rectify this the cashier himself casts the Sales Day Book, and undercasts the same to the extent of £25. The result of this would be that sales would be credited with £25 less than the proper figure, thereby compensating for the previous excess that existed.

This simple illustration shows the necessity of a completely exhaustive test of the records contained in the books where the defaulting party is enabled to make entries in any of them, since a partial test might not touch either the Ledger

Account of the customer, or the particular page of the Sales Day Book where the cast has been deliberately falsified.

(e) **The Investigator's Report.** The report to the client should indicate the extent of the fraud as discovered by the investigator, and should not only show by whom the fraud was perpetrated, but also the causes which rendered the fraud possible; and with a view to preventing the occurrence of any similar fraud in the future the necessary alterations in the system of internal check in operation should be suggested.

INVESTIGATION UNDER THE PUBLIC TRUSTEE ACT, 1906.—(a) **The Public Trustee Act, 1906.** Under the Public Trustee Act, 1906, the accounts of any trust may be investigated, and this whether or not the Public Trustee is acting in connection therewith.

Prior to the passing of this Act the only means by which an investigation could be enforced was by taking action against the trustees as the result of which the Court would order the taking of an account; but since the passing of the Act an investigation can be made without resorting to litigation.

(b) **Provisions of the Public Trustee Act and Rules.** The investigation can be obtained under the provisions of Sec. 13 of the Act, which is as follows—

(1) Subject to rules under this Act, and unless the Court otherwise orders, the conditions and accounts of any trust, shall, on an application being made and notice thereof given in the prescribed manner by any trustee or beneficiary, be investigated and audited by such solicitor or public accountant as may be agreed on by the applicant and the trustees, or, in default of agreement, by the public trustee or some person appointed by him; provided that (except with the leave of the Court) such an investigation or audit shall not be required within twelve months after any such previous investigation or audit, and that a trustee or beneficiary shall not be appointed under this section to make an investigation or audit.

(2) The person making the investigation or audit (hereinafter called the auditor) shall have a right of access to the books, accounts and vouchers of the trustees, and to any securities and documents of title held by them on account of the trust, and may require from them such information and explanation as may be necessary for the performance of his duties; and upon the completion of the investigation and audit shall forward to the applicant and to every trustee a copy of the accounts, together with a report thereon, and a certificate signed by him to the effect that the accounts exhibit a true view of the state of the affairs of the trust, and that he has had the securities of the trust fund

investments produced to and verified by him, or (as the case may be) that such accounts are deficient in such respects as may be specified in such certificate.

(3) Every beneficiary under the trust shall, subject to Rules under this Act, be entitled at all reasonable times to inspect and take copies of the accounts, report, and certificate, and, at his own expense, to be furnished with copies thereof or extracts therefrom.

(4) The auditor may be removed by order of the Court, and if any auditor is removed, or resigns, or dies, or becomes bankrupt, or incapable of acting before the investigation and audit is completed, a new auditor may be appointed in his place in like manner as the original auditor.

(5) The remuneration of the auditor and the other expenses of the investigation and audit shall be such as may be prescribed by rules under this Act, and shall, unless the public trustee otherwise directs, be borne by the estate; and in the event of the public trustee so directing, he may order that such expenses be borne by the applicant or by the trustees personally, or partly by them and partly by the applicant.

(6) If any person having the custody of any documents to which the auditor has a right of access under this section fails or refuses to allow him to have access thereto, or in any wise obstructs the investigation or audit, the auditor may apply to the Court, and thereupon the Court shall make such order as it thinks just.

(7) Subject to Rules of Court, applications under or for the purposes of this section to the High Court shall be made to a judge of the Chancery Division in Chambers.

(8) If any person in any statement of accounts, report or certificate required for the purposes of this section wilfully makes a statement false in any material particular he shall be liable on conviction on indictment to imprisonment for a term not exceeding two years, and on summary conviction to imprisonment for a term not exceeding six months, with or without hard labour, and in either case to a fine in lieu of or in addition to such imprisonment.

The Provisions of the Public Trustee Rules, 1912, amplify the provisions of the Act as follows—

Rule 31.—Any application under Section 13 (1) of the Act shall be made to the Public Trustee, and notice thereof shall (unless the Public Trustee otherwise directs) be given by the applicant to every other person being a trustee or beneficiary under the trust.

Rule 32.—(1) Upon receiving any such application the Public Trustee may in his absolute discretion by notice to the applicant require that before a day to be specified in the notice such security (by deposit of a sum of money)

as he shall deem sufficient shall be given to him by the applicant for the payment of any expenses of the investigation and audit which may be ordered by the Public Trustee to be paid by the applicant personally.

(2) Where any such requirement is made no further proceedings shall be taken upon the application until the security has been given, and if the same is not given before the day specified in the notice the application shall be disallowed unless under special circumstances the Public Trustee thinks fit to extend the time for giving the security or to dispense therewith.

(3) Any sum so deposited shall be kept by the Public Trustee on deposit in his name and to a separate account at a bank until all proceedings in connection with the investigation and audit have been concluded, and thereupon the deposited sum and the interest (if any) allowed thereon by the bank shall be applied in or towards payment of any expenses of the investigation and audit which may be so ordered to be paid by the applicant personally, and the balance (if any) shall be paid to the applicant.

Rule 33.—The Public Trustee may in his absolute discretion upon the application of any trustee or beneficiary direct that the investigation and audit shall extend only to a specified period of time or to a specified part of the trust property or shall be otherwise restricted.

Rule 34.—If within one month from the date of the application under Section 13 (1) of the Act no solicitor or public accountant shall have been appointed by the applicant and the trustees to conduct the investigation and audit, there shall be deemed to be a default of agreement within the meaning of the said Section 13 (1) and the applicant may apply to the Public Trustee accordingly.

Rule 35.—The remuneration of the auditor and the other expenses of the investigation and audit shall be such as may be determined by the Public Trustee. Provided that the Public Trustee may refer the costs of any solicitor (being part of such expenses) for taxation to a Taxing Master of the Supreme Court, and in such case the amount of the said costs when taxed shall be included in such expenses.

Rule 36.—(1) Where any investigation or audit has been made, copies of the report and certificate of the auditor under Section 13 (2) of the Act and such copies of accounts and other documents as the Public Trustee may require shall be forwarded to him by the auditor, and shall be considered by the Public Trustee before giving any direction or making any order under Section 13 (5) of the Act.

(2) The expense of making and forwarding any such copies as aforesaid and the fee of the Public Trustee (within the limits prescribed by

or in pursuance of any order relating to the fees of the Public Trustee for the time being in force) shall for the purpose of Section 13 (5) of the Act be part of the expenses of the investigation and audit.

Rule 37.—(1) Before making any order under Section 13 (5) of the Act the Public Trustee shall, if any of the parties interested so desire, hear the said parties in such manner as he shall think fit.

(2) Any such order shall specify the person by or to whom any sum is to be paid and the amount of such sum; provided that such an order may direct payment of the taxed costs of any solicitor employed in connection with the investigation and audit, and such costs shall be taxed by a Taxing Master of the Supreme Court, and the amount of such costs when taxed shall be paid as if such amount had been specified in the Order.

(3) Any such Order may be enforced in the same manner as a judgment or order of the Court to the same effect.

(c) **Rights of the Investigator.** It will be seen that investigations may be placed in the hands of either a solicitor or a public accountant, referred to in the Act and Rules as the auditor. Upon appointment the investigator is entitled to have access to the books, accounts and vouchers of the trustees, and to any securities and documents of title held by them on account of the trust, and may require such information and explanations as may be necessary to the performance of his duties, and on completion of the investigation he must forward to the applicant and every trustee, a copy of the accounts, together with a report thereon, and a certificate of correctness or otherwise.

He has a right to all necessary books and documents and the trustee can make terms with him before producing them; and if they are refused he should apply by originating summons to the Chancery Division for an order for their production.

(d) **Accounts.** The investigation will be facilitated if accounts have been kept, since any errors can be adjusted thereon; but where no accounts have been kept, it is essential that the investigator should be able to prepare them since he is required to forward a copy of the accounts to the person applying for the audit, and to every trustee.

(e) **Investigation of the Accounts.** (1) **THE WILL AND ITS TERMS.** A copy of the will or trust instrument should be obtained and an epitome thereof prepared so that the terms of the will or trust instrument are completely grasped before the investigation is started. In the case of a will it will be necessary to note all points relating to the accounts, particularly as regards legacies and devises, specific trusts, and investments authorised.

Any directions as to carrying on the business;

payment of gaming and statute-barred debts; instructions as to dealing with annuities; or the allocation of specific property for the payment of debts should also be noted.

(2) **PRIVATE BOOKS OF THE DECEASED.** In the case of the estate of a deceased person, it is desirable if possible to examine his private books (if any) to ensure that all assets in the possession of the deceased at the date of death have been brought into account. The particulars contained therein can be checked on to the Estate Duty Account, and inquiry should be made as to any assets shown in such books which are not included therein.

(3) **THE ESTATE DUTY ACCOUNT.** In the case of the estate of a deceased person, a copy of the Estate Duty Account should also be called for. This will show the whole of the property left by the deceased so far as it is aggregable for estate duty, and also all the liabilities allowed in determining the assessment. It will also show the amount of funeral expenses allowed, and the total aggregate value of the estate.

The rate of estate duty will also be shown and the amount of duty payable and any interest thereon. All these particulars should be checked by evidence available, and the calculation of duty also checked, and the account will then serve to vouch the opening Journal entries.

Any corrective affidavit should also be dealt with in the same manner, and it should be seen that the Journal entry in respect thereof is properly made.

(4) **THE OPENING ENTRIES.** The opening entries are usually made from the Journal. Assuming this has already been checked, the postings made therefrom should be verified, the Estate Duty Account being credited with the value of all assets originally appearing in the books, and debited with the total of the liabilities for which accounts will be opened.

Where investments at the date of death are quoted cum. div. it should be seen that the accruing dividend is not brought into the Estate Duty Account in addition to the price, since the valuation includes such accruing dividend as well as the capital. The dividend when received will, of course, have to be apportioned under the Apportionment Act, but the capital portion, instead of being credited to the Estate Account, must be utilised for the purpose of adjusting the capital value of the asset.

(5) **INVESTIGATION OF THE CASH BOOK.** The Cash Book will have been written up from the counterfoils of the Paying-in Book, and the counterfoils of the cheque books. The receipts will be vouched by reference to the following documents—

(a) For sale of investments: brokers' sold notes.

(b) For sale of property by auction or private treaty: auctioneers' accounts, solicitors' letters, etc.

(c) Dividends, interest, etc.: counterfoils of dividend and interest warrants, reference to scrip, etc.

(d) Rents, from the counterfoil of the Rents Receipt Book, or agents' rental return.

(e) Debts due to testator: from the press copy Letter Books and any other evidence available.

The payments will be vouched by reference to the following documents—

(a) For purchase of investments: brokers' bought notes.

(b) For estate duty: the probate of the will.

(c) For other payments: the usual vouchers.

(d) For payments to legatees: legal receipts which must be properly stamped with the amount of the duty.

(e) For payments to annuitants: receipts therefor, and also receipts for the legacy duty thereon.

Where legacies are not left free of duty it must be seen that the duty has been deducted from the legacy before payment to the legatee, the amount of the duty paid to the Inland Revenue authorities making up the full amount of the legacy.

The Cash Account when completed and vouched, should be cast, and the balance in hand agreed with the Bank Pass Book, a certificate for the balance being obtained from the banker.

In vouching payments for executorship expenses it must be seen that such expenses are reasonable and proper. An executor or trustee is not entitled to charge for his services unless the will or trust instrument authorises him to do so.

(6) **APPORTIONMENTS.** Apportionments are necessary for the following reasons—

(a) In the case of the estate of a deceased person to determine accurately the estate duty payable.

(b) In the case of a trust to adjust the rights of the parties interested in the estate, e.g. life tenants and remaindermen.

(c) In either case to determine correctly the incidence of charges and expenses.

The object of apportionment is to allocate receipts or expenses to capital or income in the proper proportions.

Receipts are apportionable under the Apportionment Act, 1870, that part of income accruing up to the date of death being treated as capital, and the part which accrued after death being treated as income; while moneys received after death may also be apportionable under case law, e.g. the rule in *Howe v. Lord Dartmouth*, 1802, 7 Ves. 137; the rule in *re The Earl of Chesterfield's Trusts*, 1883, 24 Ch.D. 643; the rule in *re Atkinson*, 1904, 2 Ch. 160, etc., a certain portion of such receipts being due to capital and a portion to income.

Apportionments of moneys received under the Apportionment Act, 1870, are known as statutory apportionments, and are made purely on a time basis, whereas those made under case law are known as equitable apportionments and are made on an equitable basis.

Expenses may be apportionable under statute, e.g. under the Settled Lands Acts, 1882-1890, or under case law, e.g. under the rule *in re Perkins*.

In the case of a trust, apportionments may be necessary where unauthorised investments are retained; since in the case of wasting or hazardous investments which are not authorised by the trust instrument, it is necessary that an equitable apportionment of the income should be made for the benefit of capital.

The following are some of the principal rules with regard to apportionments—

(a) Under the Apportionment Act, 1870, all rents, annuities, dividends and other periodical payments in the nature of income (whether reserved or made payable under an instrument in writing or otherwise) shall, like interest on money lent, be considered as accruing from day to day, and shall be apportionable in respect of time accordingly.

(b) Under the rule in *Howe v. Lord Dartmouth*, 1802, 7 Ves. 147, where a residue is bequeathed to two or more persons in succession, and all or part thereof consists of assets of a wasting or hazardous nature, it is the duty of the executors, subject to the terms of the will, to convert the wasting or hazardous property into money and invest the proceeds in authorised securities. Where the conversion is made within a year of death, the tenant for life is entitled out of the income to 3 per cent. on the actual net proceeds of such conversion. Where it is of such a nature that it cannot be converted within a year of death without heavy loss being incurred, the tenant for life is entitled to 3 per cent. on the capital value of the property as at the date of the testator's death. If the property could have been converted during the year without difficulty, but has been retained at the discretion of the executors, the tenant for life is entitled to the proceeds of such an investment in Consols as could have been acquired by money representing the value placed upon the property at the expiration of one year from death. The balance of income derived from the property is capitalised in each case, and goes to increase the corpus of the estate.

(c) As in the case of the *Earl of Chesterfield's Trusts*, 1883, 24 Ch.D. 643, where part of the residue consists of outstanding personal estate, apportionment must be made when the property actually falls into possession, or is realised, and it is then necessary to ascertain what sum invested at 3 per cent. compound interest on the day of the testator's death would, on the day when the

property does fall in or is realised, amount to the value of the sum actually received. The sum so ascertained is capital, the balance income.

(d) In the case of *Allhusen v. Whittell*, 1867, L.R. 4 Eq. 295, it was decided that that portion of the estate which was required to enable the debts, funeral expenses, and legacies to be paid, was not to be deemed as part of the true residue of the estate, and in consequence the life tenant is not entitled to income from that portion of the capital which is required for these payments. To comply with the rule in this case, it is necessary to set aside out of capital a sum which, with interest for the year succeeding death, will amount to the total required to pay the debts, funeral expenses, and legacies, income providing the amount so attributable to interest, and capital the remainder.

Interest at 4 per cent. may, however, now be charged against income for the period from the date of death till the date of payment, under the decision given in *re McEuen*, 1913, 2 Ch. 716, the whole payment being first charged against capital.

(e) In the case of *re Atkinson*, 1904, 2 Ch. 160, it was decided that where a loss is sustained on the realisation of a mortgage security, both principal and interest must bear their portion of the loss. The rule is to aggregate the principal and all arrears of interest to date of realisation, and the amount realised must then be divided in the ratio that the principal and the arrears of interest bear to the aggregation respectively.

(f) In the case of *re Perkins*, 1907, 2 Ch. 596, it was decided that where a testator had made himself liable to pay an annuity and leaves same as a charge upon the residue of his estate, it must be ascertained as each payment of the annuity becomes due, what sum invested at 4 per cent. simple interest on the date of the testator's death would produce the instalment of the annuity due. The sum so found will be chargeable to capital, and the balance to income.

In all cases of the equitable apportionment of income the life tenant is only entitled to be paid out of the income; and in any case a statutory apportionment must be made in respect of income arising during the period in which the death took place.

In the case of wasting or fluctuating assets specifically settled without any trust for conversion, the life tenant is entitled to income actually produced during his life tenancy, and this notwithstanding any power given to the trustees to vary securities. Also in the case of settled residue the rule in *Howe v. Lord Dartmouth* will not apply where the particular property is settled in such a way that the life tenant is to enjoy in specie. But where the property is settled by will, by way of trust for sale, and no provision is made as to the intermediate income, the life

tenant is only entitled to so much as would have been produced if the property had been realised one year after death, and invested in Consols, the balance of the income then being capitalised.

In cases of difficulty where large sums are at stake, it may be desirable for the opinion of counsel to be taken, and if necessary an order of the Court can be obtained as to the correct apportionment by taking out an originating summons.

(7) RENTS. If a rent-roll be kept, whether by the executors or trustees, or by an agent, the same must be checked up with the terrier of the property, and counterparts of tenants' leases and agreements.

The essential details would be the particulars of the property, annual rental, arrears, total sum due, amounts paid, allowances, repairs, balance outstanding.

Allowances and expenditure on repairs must be vouched, care being taken to ensure that the latter has been duly authorised.

(8) CARRYING ON THE BUSINESS. Where the business of a deceased person is being carried on by his executors, either in accordance with the instructions in the will, or for the purpose of being wound up, accounts should have been taken at the date of death to ascertain the exact position of the business, and these should be examined. It would be necessary to audit the accounts of the business since the date of death.

It should be remembered that except for the purpose of beneficially winding up the business, there is no power to carry on a business unless express directions are given by the will. In the absence of a distinct and positive authority to this effect, the executor is personally responsible for debts incurred, with no right to be reimbursed out of the estate. If there be an authority to carry on the business he will still be personally liable for debts incurred, but will be entitled to be indemnified out of specific assets which he is authorised to employ.

It may happen, however, that though the will confers no authority to carry on the business, the executor is entitled to indemnity if the beneficiaries or even the creditors of the deceased were aware of the fact and tacitly assented thereto.

(9) INVESTMENTS. Investigation should be made into the character of the investments representing the estate. The executor or trustee is only entitled to invest the trust moneys in such investments as are authorised by the will or trust instrument, or by the Trustee Act, 1893, or Colonial Stock Act, 1900. Where unauthorised investments are made or retained without authority, it is essential that the income arising therefrom should be subjected to an equitable apportionment as already explained.

The executors or trustees will be responsible

personally for any devastavit occasioned by improper investments.

(10) SPECIFIC TRUSTS. If separate trusts are created under a will or the trust deed, it should be seen that these are properly recorded in the books, and that specific investments made in respect thereof are duly earmarked against such trusts. If the trust is on behalf of minors the income arising therefrom should be dealt with in accordance with the will or the trust instrument, or the directions of the Court as the case may be.

(11) VERIFICATION OF ASSETS. It is necessary that all the assets should be actually verified. The balance at the bank should be verified by obtaining a certificate from the bank as to the amount thereof at the particular date to which the investigation is taken. Title deeds should be actually examined, and so also should share certificates, stock certificates, etc. If inscribed stocks are held, letters of verification should be obtained in respect of these from the bank of inscription.

Where investments are registered in the name of a sole executor or trustee, a certificate should be obtained from him that he holds same on behalf of the estate or trust free of any encumbrances.

It must be remembered that the investigator is required under the Act to certify that he has had the securities of the trust fund investments produced to him and verified by him or otherwise (as the case may be).

(12) THE INCOME ACCOUNT. The income from the various investments will have been proved in the course of the investigation, and it will have been seen whether or not all income that ought to have been received has actually come to hand. These items will be transferred to the credit side of the Income Account, and against them will be charged all payments in the nature of income expenditure, and the balance will be transferred to the credit of the Beneficiaries Accounts in their proper proportions.

It is not necessary to take accrued income into account, but it is advisable to bring into account all accrued expenses.

(13) THE BALANCE SHEET. The Balance Sheet should be prepared at the date to which the investigation is taken, and should show all the assets of the trust on one side and on the other side any liabilities, whether to creditors or to beneficiaries, and the Capital Account of the trust.

The Balance Sheet should be so drawn up that it shows the exact position of affairs of the trust at the date specified.

(14) DEVASTAVIT. If any devastavit has been committed it would be necessary to bring such matters to light in the report which must be prepared and forwarded to the person who applied for the investigation, and to every trustee.

A devastavit is a wasting of the assets which may have taken place in various ways, *e.g.* by an improper distribution of all the income arising from unauthorised securities, a loss of capital in respect of unauthorised securities, a loss of the trust assets caused by carrying on a business without authority.

(15) CERTIFICATE. The investigator must forward to the party applying for the investigation, and to every trustee, a copy of the accounts duly certified by him, together with a report thereon. The form of certificate will be as follows—

"I hereby certify that the above accounts exhibit a true and correct view of the state of the affairs of the — Trust, and that I have had the securities of the Trust Fund Investments produced to me, and that I have verified the same";

or will give particulars of any matters in respect of which the accounts are incorrect or the production of securities is deficient, or will refer to the report in which these matters are stated.

THE LIABILITY OF THE INVESTIGATOR.—

All professional men are liable for any negligence which they may show in the conduct of their professional work, but this is only to the persons from whom they receive the mandate to perform that work. So far as negligence is concerned, therefore, the liability for this arises out of contract, and only the other party to the contract will be able to sue the investigator if negligence be charged.

In view of the fact that the person making the investigation can be charged with negligence or want of skill in carrying out his professional work, it behoves all professional accountants conducting investigations to exercise that skill and intelligence which has been set up, as it were by an evolutionary process, during that period which has seen the making of the accountancy profession. It is, therefore, necessary for every accountant conducting an investigation to approximate as far as he can to the highest ideals in such matters.

What negligence is would be difficult to define generally; it would depend upon the particular circumstances of the case. It is a question of fact, and where litigation results, the method of determining the facts will be the ascertaining of what has been done, and the calling of expert evidence by both sides to the action to prove what independent experienced persons consider should have been done having regard to their experience in similar matters.

In any case, so far as negligence is concerned, *i.e.* the performance of professional work without the exercise of proper skill, care and caution, the only liability is to the other contracting party, this liability arising out of contract.

It must not be overlooked, however, that there may be a liability to third parties, where the

investigator has deliberately misrepresented matters with the intention that the misrepresentation shall be acted upon by the third party. This involves an action for tort, and to be successful fraud must be proved.

In view of the fact that the investigator is always liable under his contract to exercise care, skill and caution, and in view of the possibility of the further charge in an action of tort, it is of the utmost importance that he should always record in his private books the fullest possible information; so that he can substantiate any statement which he may have made, whatever charge may be brought against him.

These notes will also be of the greatest utility should any further information or explanations be required after he has made his report upon any investigation which has been placed in his hands.

INVESTMENT ACCOUNTS.

It is important that the transactions relating to investments should be so recorded that the position of each can be clearly seen. With this end in view a separate account should be kept for each investment, or, if the number of investments warrants it, a separate ledger might be kept. The form of account differs somewhat from the ordinary ledger account, in that it usually has three columns on each side. In the first of these is shown the nominal amount and the stocks or shares which the investment represents, the second column is used for interest or dividends, and the third for principal. This arrangement is desirable owing to the fact that the interest or dividends (revenue) must be kept distinct from the principal (capital). When opening an account it is necessary first to ascertain if there is any accrued interest. If there is, this should be entered in the interest column and the balance of the purchase money (representing the actual capital cost of the investment) in the principal column. The nominal amount of the investment will also be entered in the appropriate column. As the dividends or interest is received it is posted, less tax, to the credit of the account in the interest column. In the event of a sale of an investment it will again become necessary to distinguish between interest and principal, the amount of the accrued interest (*i.e.* the interest which has been earned between the date of last dividend and the date of the sale) which is included in the selling price, being entered in the credit interest column, and the balance of the selling price in the credit principal column. The amount thus entered in the principal column shows the actual amount of capital included in the selling price. At the end of a financial period the interest is transferred to the profit and loss account, but before doing this credit should be taken for any interest accrued

EXAMPLE 1.]

2½% CONSOLS

Dr.										DIVIDENDS PAYABLE ON 5TH JAN., 5TH APRIL, 5TH JULY, AND 5TH OCT.										Cr.									
Date.		Particulars.		Nominal Value.		Dividends or Interest.		Capital or Principal.		Date.		Particulars.		Nominal Value.		Dividends or Interest.		Capital or Principal.											
		£	s. d.	£	s. d.	£	s. d.	£	s. d.			£	s. d.	£	s. d.	£	s. d.	£	s. d.										
19..	To Balance	5,200	0 0	21	10 3	4,168	11 0	19..																					
Jan. 1	By Cash—							Jan. 5																					
Dec. 31	„ Transfer to Dividends and Interest Account			91	0 0			Qr's. Dividend to date £32 10																					
								Less tax at 6s. 9 15														22	15 0						
								April 5 „ Cash (do.) . . .														22	15 0						
								July 5 „ „ „ . . .														22	15 0						
								Oct. 5 „ „ „ . . .														22	15 0						
								Dec. 31 „ Balance c/d . . .												5,200	0 0	21	10 3	4,168	11 0				
		5,200	0 0	112	10 3	4,168	11 0													5,200	0 0	112	10 3	4,168	11 0				
19..	To Balance	5,200	0 0	21	10 3	4,168	11 0																						
Jan. 1																													

NOTE 1.—The accruing dividend at the beginning of the year is obtained by taking $\frac{2}{5}$ of £22 15s., and the same amount will be carried forward again at the end of the year.

NOTE 2.—Some accountants make the apportionment on the dividend for the whole year, thus— $\frac{2}{5}$ of £91. This works out to £21 13s. 9d., a variation of 3s. 6d. It makes no difference, however, in the yearly income, which remains at £91 whichever way is adopted.

EXAMPLE 2.]

4% BLANK CONSOLIDATED STOCK

Dr.

DIVIDENDS PAYABLE ON 31ST MARCH, 30TH JUNE, 30TH SEPT., AND 31ST DEC.

Cr.

Date.	Particulars.	Nominal Value.		Dividends or Interest.		Capital or Principal.		Date.	Particulars.	Nominal Value.		Dividends or Interest.		Capital or Principal.	
		£	s. d.	£	s. d.	£	s. d.			£	s. d.	£	s. d.	£	s. d.
19.. Mar. 1	To Cash— Purchase of £12,000 at 90 cum div. plus Brokerage $\frac{1}{4}$ th and Stamps and Expenses, £5 8s. .	12,000	0 0	56	0 0	10,764	8 0	19.. Mar. 31	By Cash— One Qr.'s Dividend on £12,000 £120 Less tax at 6s. 36			84	0 0		
Dec. 31	„ Profit on Sale of Investments Account (transfer) . .					90	12 0	June 1	„ Cash— Sale of £3,000 at 92 cum div. less Brokerage $\frac{1}{4}$ th and Expenses, 27s. .	3,000	0 0	14	0 0	2,740	18 0
„ „	„ Dividends and interest Account (transfer) . .			203	0 0			„ 30	„ Cash— One Qr.'s Dividend on £9,000 £90 Less tax at 6s. 27			63	0 0		
								Sept. 1	„ Cash— Sale of £3,000 at 91 exd div. less Brokerage $\frac{1}{4}$ th and Expenses, 27s. .	3,000	0 0			2,724	18 0
								„ 30	„ Cash— One Qr.'s Dividend on £9,000 £90 Less tax at 6s. 27			56	0 0	*7	0 0
									£63						
								Dec. 31	„ Cash— One Qr.'s Dividend on £6,000 £60 Less tax at 6s. 18			42	0 0	5,382	4 0
								„ „	„ Balance (at cost) c/d	6,000	0 0				
		12,000	0 0	259	0 0	10,855	0 0			12,000	0 0	259	0 0	10,855	0 0
19.. Jan. 1	To Balance b/d . .	6,000	0 0			5,372	10 8								

* £3,000 Stock was in hand only 2 months; therefore 1 month's dividend on it must be credited to Capital. Where Dividends are not at a fixed rate, adjustments can only be made when the Dividend is actually received.

to the date of balancing. This is credited to the investment account in the interest column and debited to an interest accrued account; or it may be brought down in the investment account itself as a debit balance. The interest columns are then balanced, and the balance carried to the dividend and interest account, and thence to the profit and loss account.

With regard to the principal columns, if the investment remains intact the amount is simply brought down as a debit balance to the new period. If part only of the investment has been sold, the remainder is valued at cost, credited to the investment account, and brought down to the debit of the new period. The principal columns are balanced and the difference represents either the profit or loss on that part of the investment which has been disposed of. If the whole of the investment has been sold, any balance remaining in the principal column is the profit or loss on the sale, and although it is a capital profit or loss, it is usually transferred to the revenue or profit and loss account.

It may be mentioned that unless otherwise stated investments are bought or sold *cum div.* If the price does not include the dividend or interest it is usually marked *ex div.* The two following examples adapted from *Pitman's Dictionary of Book-keeping* will illustrate the method of keeping the accounts.

Example 1. A. Brown holds £5,200 of 2½ per cent. consols which cost him, including brokerage and expenses, £4,166 11s. 0d. Show the ledger account for one year, dividends being payable on the fifth day of the first month of each quarter of the year. (See page 594.)

Example 2. A Company purchased on the 1st March, 19... , £12,000 of 4 per cent. Blank Consolidated Stock at 90, dividends being payable on the last day of each quarter of the year. Brokerage was charged at the rate of ¼th per cent., and stamps and expenses amounted to £5 8s. 0d. On 1st June £3,000 of stock was sold for cash at 92, less brokerage ¼th and expenses £1 7s. 0d. On 1st September another £3,000 of stock was sold for cash at 91 *ex div.*, less brokerage ¼th and charges £1 7s. 0d. The market price on 31st December, the date of the Balance Sheet, was 89. Show the ledger account of the investment recording the above transactions and the receipt of the quarterly dividends, and balance it as on 31st December. (See page 594.)

INVESTMENTS.

(See ACCOUNTS, CRITICISM OF, p. 18; AUDITING, pp. 93, 99; BALANCE SHEET, p. 145.)

INVESTMENTS, DEPRECIATION OF.

(See DEPRECIATION.)

INVESTMENTS, PROFIT [AND LOSS ON.

(See EXECUTORSHIP ACCOUNTS.)

INVESTMENTS, RESERVE.

(See BALANCE SHEET, p. 142.)

INVESTMENTS, VERIFICATION OF.

The verification of investments usually takes place once a year as part of the audit of the accounts of companies, public bodies, landed estates, trustees, or partnerships etc. In the case of banks, discount houses, insurance and financial companies or trustees, it is generally a considerable part of the auditor's duties.

For obvious reasons, it is desirable that, as far as practicable, the process of verification commence at the close of business on the balancing day, and be completed with the greatest possible dispatch.

Bills and securities liable to be exchanged or varied frequently, such as "cover for short loans," should be examined in the first place.

If the verification does not take place on the last day of the year, and any changes have in the meantime been made in the nature of any of the investments, the variations, including, for example, proceeds of sales, if any, should be traced through the books.

To avoid substitution, the whole of the documents representing the investments should be produced to the auditor at the same time. This may be achieved by giving him, during his examination, complete control of the strong rooms and safes containing the documents, cash, etc.; or joint control by the auditor and his client may be arranged, each party placing his seal on the doors of the strong rooms or safes during such time as the examination is suspended.

As to securities in general, the auditor should have before him a complete list of the documents which he ought to see, as shown by the books (duly audited), or the books themselves, and should see that the documents correspond with the entries in the lists or in the books as to principal, interest, terms of repayment and description of security, etc. Bankers and cash balances should be agreed with the balances of the Cash Books.

Where, as sometimes happens, leases, certificates or other documents are in the names of persons other than the actual owner, a letter of acknowledgment or transfer in blank signed by the nominal holder should be produced.

The auditor should satisfy himself that the investments are within the power of the company, public body or trustees, as the case may be, and also within the powers of those who purport to act on their behalf.

The investments (including those held as securities for loans) may comprise—

Debentures, Bonds, etc.

Title Deeds, including Mortgages, Leases, etc.

Stocks and Shares—

(a) Inscribed ;

(b) Registered.

Trade Documents.

Temporary Investments.

Life Assurance Policies, Life Interests and Reversions.

Loans to Public Bodies.

Patents and Trade-marks.

Bills of Exchange.

Deposits at and Accounts Current with bankers, also cash balances, including bank notes.

Strictly speaking, the last items are not investments or securities, but they are usually included, as they must necessarily be verified at the same time.

DEBENTURES.—The debenture trust deed, debentures, debenture certificates, or bonds to bearer should be produced. These documents should bear a copy of the Certificate of Registration within the prescribed time at Somerset House. Where there are coupons attached to the debentures or bonds, the auditor should see that those for the payment of interest next due have not been removed.

TITLE DEEDS.—At the first audit, the auditor should have all the documents mentioned in the "Abstract of Title" (which gives full particulars of all the transactions up to the last conveyance) produced to and verified by a solicitor. Having in this way, once and for all established the authenticity of the documents, then, provided they are marked for the purpose of identification, the production of the same deeds in future years ought to be sufficient. As a rule, however, directors, executors, and other clients would raise an objection to the examination of the title deeds beyond the last conveyance, in which case an auditor for his own protection would refer to the fact in his report or letter sent with the accounts.

The all-important document, however, is the latest conveyance, being the one into the names of the company, trustees or others, whereby the legal estate vests. In the case of a mortgage the conveyance to the mortgagee should be produced, unless it is incorporated in the mortgage.

There may also be what is called an equitable mortgage, that is, a deposit of title deeds as security for a loan, accompanied frequently by a memorandum of deposit, which, if executed after 1907, should bear an *ad valorem* stamp at the rate of 1s. per cent. In such a case, the auditor should see the memorandum and the conveyance vesting the legal estate in the borrower. The unsatisfactory feature of this form of security is that an

equitable mortgage does not vest the legal estate in the lender, and is, therefore, postponed to a subsequent mortgage deed, vesting the legal estate in another lender. In the case of companies, even an equitable mortgage requires registration as a "charge" at Somerset House, pursuant to Section 93, Companies (Consolidation) Act, 1908.

In the case of properties, the fire insurance policies and the receipt for the last premium should be produced.

For the purpose of identifying the properties mentioned in title deeds, the rent-roll relating to same may be inspected.

Where properties have been mortgaged and the title deeds are in other hands, a letter should be obtained from the mortgagee giving the amount of the loan and particulars of the charge he holds.

STOCKS AND SHARES.—(a) **Inscribed.** This class of stocks consists of Consols, certain other Government and Municipal Stocks, which are inscribed at the Bank of England, the Crown Agents for the Colonies, or the leading joint stock or private banks. The stocks are inscribed in the names of the holders, in books kept for the purpose by the Inscribing House, and can only be transferred by the signature of the holders or their attorneys in such books—no certificates being issued. Forms for the purpose of verification are issued by the banks. The forms embody certificates to the effect that on the date in question the stocks detailed on the form stood in the names of the holders. The form, before being sent to the bank for certification, has to be signed by at least one of the stockholders. After completion by certification, the form should be sent direct to the auditor. The process is repeated at each audit, a separate form being required each year. The memorandum as to the fact of inscription in certain names, which is often retained by the stockholders and deposited with the securities, is of no value as evidence, and should be disregarded.

The following are a reproduction of the forms in use by—

The Bank of England. (Form 1.)

The Crown Agent for the Colonies. (Form 2.)

The London County Westminster and Parr's Bank, Limited. (Form 3.)

Where no forms are supplied, a letter is usually addressed to the Inscribing House, accompanied by an authority from the stockholders to give the required information.

(b) **Registered.** Share certificates or warrants should be produced, care being taken that they are certificates without the deposit of which a transfer will not be accepted. They should be filled up in the name of the party owning the security. The amount paid up in respect of the shares is usually stated on the face of the share

CROWN AGENTS FOR THE COLONIES
WHITEHALL GARDENS, LONDON, S.W.

FEE ENCLOSED
 £ : s. d.
 By { Cheque
 Postal Order
 Stamps

This Application must be forwarded to the Crown Agents for the Colonies two days before the verification is required, accompanied by Stamps or Postal Orders for the requisite Fee, viz., 6d. per Account, with a minimum of 1s. per Certificate.

The particulars must be filled in by the applicant, and if there is more than one Account, the aggregate total must be shown at foot.

Address to which the Certificate should be sent :—

M _____

of _____

-----19-----
----- hereby authorise this application.

To be signed by a Stockholder in each account; or, in case of a Corporation, by the Chairman, Secretary, or other Officer.

At the close of business on the _____ day of _____ 19____,
the undermentioned amounts of Stock were standing in the names against which they
are placed.

Names of Stockholders.	Amounts.			Names of Stocks.

The fee payable to the LONDON COUNTY WESTMINSTER AND PARR'S BANK on verification of Stock Accounts is 6d. per Account, with a minimum charge of 1s.—such fee to be remitted with this application.

ALL COMMUNICATIONS
TO BE ADDRESSED TO
THE MANAGER,
COLONIES AND AGENCIES
DEPARTMENT,
41 LOTHBURY, E.C.2

(3.)

-----19---

TO THE
LONDON COUNTY WESTMINSTER AND PARR'S BANK LTD.,
HEAD OFFICE,
COLONIES AND AGENCIES DEPARTMENT,
41 LOTHBURY, LONDON, E.C.2

PLEASE USE
COPYING INK.

GENTLEMEN,

Be pleased to certify that on the-----the
undermentioned amounts of Stock were inscribed in the names specified in the
Books kept by the London County Westminster and Parr's Bank, Limited,
as Registrars of the Stocks, and forward the Certificate to-----

I am, GENTLEMEN,

Your obedient Servant,

To be signed by one of }
the Stockholders. }

Names of Stockholders.	Amount of Stock.	Description of Stock. (Full title and redemption date must be stated.)

(4 .)

BALANCE TICKET

[COUNTERFOIL.]

THE FOREIGN CONCESSIONS COMPANY, LTD.,
FINSBURY BUILDINGS, LONDON, E.C.2

The Shareholder mentioned below is entitled to the Shares hereunder specified—

No. of Certificate-----

Name of Shareholder-----

Number of Shares due on Balance-----

Distinctive numbers (all inclusive)-----

Balance Ticket issued to-----

Date of issue-----

Secretary.

NOTE.—No Transfer for any of the above Balance of Shares can be certified without the production and surrender of this Receipt. The Certificate for the balance of the above Shares will be ready for exchange on any day at the expiration of Seven days from this date, from 11 a.m. to 4 p.m. (Saturdays excepted). If part only of the above Shares should be sold before a new Certificate is issued, a fresh Balance Ticket will be given.

.....
BALANCE TICKET

THE FOREIGN CONCESSIONS COMPANY, LTD.,
FINSBURY BUILDINGS, LONDON, E.C.2

The Shareholder mentioned below is entitled to the Shares hereunder specified—

No. of Certificate-----

Name of Shareholder-----

Number of Shares due on balance-----

Distinctive Numbers (all inclusive)-----

Balance Ticket issued to-----

Date of Issue-----

Secretary,

NOTE.—No Transfer for any of the above balance of Shares can be certified without the production and surrender of this Receipt. The Certificate for the balance of the above Shares will be ready for exchange on any day at the expiration of Seven days from this date, from 11 a.m. to 4 p.m. (Saturdays excepted). If part only of the above Shares should be sold before a new Certificate is issued a fresh Balance Ticket will be given,

(5.)

TRANSFER DEED RECEIPT

[COUNTERFOIL.]

THE FOREIGN CONCESSIONS COMPANY, LTD.,
FINSBURY BUILDINGS, LONDON, E.C.2

RECEIVED Transfer Deed as under— No.-----
No. of Deed----- (No. of Certificate-----)
Transferor----- (for ----- Shares)
Transferee-----
No. of Shares-----
Deposited by -----
Fee paid -----
Date -----

Subject to the approval of the Directors.

For THE FOREIGN CONCESSIONS COMPANY, LTD.,

Secretary.

NOTE.—This Receipt is exchangeable for Transferee's Share Certificate at the expiration of Seven days from this date from 11 a.m. to 4 p.m. daily, except Saturdays.

TRANSFER DEED RECEIPT

THE FOREIGN CONCESSIONS COMPANY, LTD.,
FINSBURY BUILDINGS, LONDON, E.C.2

RECEIVED Transfer Deed as under— No.-----
No. of Deed----- (No. of Certificate-----)
Transferor----- (for ----- Shares)
Transferee-----
No. of Shares-----
Deposited by -----
Fee Paid-----
Date -----

Subject to the approval of the Directors.

For THE FOREIGN CONCESSIONS COMPANY, LTD.,

Secretary.

NOTE.—This Receipt is exchangeable for Transferee's Share Certificate at the expiration of Seven days from this date from 11 a.m. to 4 p.m. daily, except Saturdays.

(6.)

TO THE GOVERNOR AND COMPANY
OF THE BANK OF ENGLAND.

----- request that the subjoined list of Securities may be verified.

Signature-----

Date-----

At the close of business on the-----day of-----, 19---, the
undermentioned Securities were held by the Bank of England for the account of-----

TOTAL £			

Say-----

BANK OF ENGLAND,

-----19

Exd.

Chief Cashier.

certificate. The amount paid up in respect of subsequent calls should be endorsed on the back of the certificate. Where the shares are fully paid the certificate is worded accordingly. In the case of new issues, where share certificates have still to be issued, the "Scrip," namely, the Allotment Letter, together with bankers' receipts for the amounts paid on application and allotment and calls paid, should be produced. The share certificate is only given up in exchange for those documents, or, where they are lost, for a letter of indemnity. If part of a holding has been sold, and the new certificate for the balance has not been received, a "Balance Receipt" should be produced. A common form of Balance Receipt is given on page 600.

Where shares have been recently purchased and the share certificate is not available, a certified transfer, or if the transfer has been lodged for registration, a transfer receipt from the company which has to issue the certificate in exchange therefor, should be produced. A certified transfer is a transfer bearing the following words—

Certified at the Company's Office.

Date..... Secretary.

A common form of Transfer Receipt is shown on page 601.

In some cases, mostly foreign securities, the transfer of shares is simply endorsed on the back of the share certificate.

As a further precaution, it is always open to the auditor to inspect the register of the companies in which Registered stocks and shares are held and see that the register and the certificate tally—but this is seldom considered necessary.

Where securities are in the hands of a banker of repute, a letter from the banker giving details of the securities held is sufficient. The Bank of England form of certificate in such cases is as shown on page 602.

TRADE DOCUMENTS.—These would include, in the case of goods in transit, bills of lading, marine insurance policy, and invoice relating to the goods; in the case of goods in warehouse, the invoice, the usual warrants to order, and a fire insurance policy.

TEMPORARY INVESTMENTS.—Temporary Investments are usually in respect of moneys liable to be called in at short notice, or moneys awaiting a permanent investment. The two principal investments of this nature are—

(a) **Money Deposited with a Discount Company or Financial House.** In this case a certificate from the company or house with whom the money is deposited should be obtained:

(b) **Loans to Stockbrokers and Others against Security.** The securities deposited "as collateral" in these cases should be capable of transfer by delivery, as, for example, bonds or stocks to

bearer. The documents should be produced together with a Memorandum of Deposit or an account showing the amount advanced.

LIFE ASSURANCE POLICIES, LIFE INTERESTS AND REVERSIONS.—The policies should be produced, also receipt for the last premium due, and deeds of assignment, if any, relating to same.

In the case of life interests and reversions, the deed of assignment should be produced, also any policies to cover reversionary contingencies. The auditor may also take means to satisfy himself that due notice of the assignment has been given.

In the case of assurance companies, where the companies have made advances within the surrender value of the policies, the auditor should see the deeds relating to the loan, and also the policies. In practice, it is sometimes considered sufficient to see a substantial number of these documents picked out at random.

LOANS TO PUBLIC BODIES.—The auditor should see the deed by the local authority relating to the loan (in which the receipt for the principal sum is embodied) and see that the periodical repayments (if any) stipulated for therein have been duly made and accounted for.

PATENTS AND TRADE-MARKS.—In the case of patents, see patent and receipt for last payment due in respect of renewal fees, described as Certificate of Payment or renewal. In the case of trade-marks, see Certificate of Registration.

BILLS OF EXCHANGE AND PROMISSORY NOTES.—It is only in the case of bankers and discount houses that one is likely to find many bills on hand. The bills should be checked at the close of business on the last day of the company's year, and agreed with the Bill Books and the corresponding Ledger balance. Bills held as security for advances, which should be in separate portfolios, must be examined in the same way. Bills sent for collection should be duly traced and accounted for. In the case of trading concerns, the bills receivable have usually been discounted. Those on hand should be examined and the total agreed with the balance of Bills Receivable Account and the details in the Bills Receivable Book.

DEPOSITS AT AND ACCOUNTS CURRENT WITH BANKERS, NOTES AND CASH BALANCES.

—Deposits at bankers should be verified by the production of the deposit receipt, or by a letter from the bankers. As a further check, the receipt of the interest on the deposit should be traced in the books.

As to the current accounts, one side of the company's, trustees' or other accounting party's Cash Book should be compared in detail with the corresponding side of the Bank Pass Book. The balance of the Cash Book and Bank Pass Book should be reconciled, allowance being made for

outstanding cheques, the castings on both sides of the Cash Book checked, and the balance as shown by the Pass Book verified by a letter from the bankers. Below is the form in use by the Bank of England.

Cash should be counted or weighed. In the case of banks, this is done at the close of business on the last day of each year. In other cases, the amount of cash in hand is not usually of importance, and, where practicable to do so, it should be paid into the bank at the close of business on the last day of the financial year, a fresh cheque being drawn on the following morning to replenish the till or float.

Notes should be arranged according to their amounts and then counted. (See also AUDITING, p. 97.)

INVOICE.

An invoice is a document giving full particulars of goods purchased, including quantities, prices and totals for each class or quality of goods, the total of the whole purchase being also shown. (See also INVESTIGATIONS, p. 586.)

INVOICE BOOK.

A book for the first entry of particulars of goods purchased, and may be either an Invoice Guard Book (see GUARD BOOK), or a Purchases Book (Purchase Day Book, Purchase Journal), the latter being the more convenient form. The book

should be ruled to provide columns for number of invoice, date, the name of the person from whom the goods were purchased, Ledger folio, and amount. The invoices being filed in numerical order, reference to them for full particulars of the purchase may be easily made, and only the total amount of the purchase need be entered, although in some businesses it is deemed advisable to copy the invoices in full into the book.

The individual entries are posted to the credit of the Personal Accounts in the Credit Ledger, and the totals of the book posted at such periods as may be desired to the debit of the Purchases Account in the Nominal Ledger.

In the case of departmentalisation, analysis columns for the goods purchased on account of each department may be provided, and in the case of the firm's Ledgers being sectionally balanced, columns must be adopted for each Credit Ledger.

The Invoice Book is sometimes arranged for the recording, not only of goods purchased, but of all transactions on credit, in which case it is provided with columns for the analysis of the entries under appropriate Nominal Ledger headings, such totals being posted periodically to the Nominal Ledger Accounts, a separate book being used by some firms for transactions on account of expenses. (See also SELF-BALANCING LEDGERS, p. 848.)

INVOICES, CHECKING OF.

(See DEPARTMENTAL STORES, p. 381.)

(7.)

Balance standing to the credit of the account of_____

on the evening of the_____

£_____

BANK OF ENGLAND,

Examined.

Chief Cashier.

INVOICES DATED FORWARD.

The practice of dating forward invoices is a source of danger, particularly when the dating forward covers the date of stocktaking, because it sometimes leads to the goods, in respect of which such invoices are issued, being included in the stock, whilst the invoices themselves are excluded from the charges of the period, owing to the misleading date upon them. If the goods have not actually been used, the safest course is to exclude them from the stocktaking, and to omit the invoices from the record of purchases. If the goods, on the other hand, have been used or disposed of, then it is essential that the invoices in respect of them should be brought into account, whatever date they bear.

To ensure against any errors arising from this practice, the auditor should insist on the connection between the Goods Received Book and the invoices being maintained by a system of cross references, and should make a point of examining the Goods Received Book to satisfy himself that all invoices have been properly brought into account. An examination of the invoices immediately beyond the period's accounts may lead to the discovery of invoices dated forward which have been improperly excluded, whilst a reference to the Purchase Contract Books may lead to a similar disclosure.

The practice of checking creditors' statements

with the Purchases Ledger balances is also useful for the purpose of discovering the omission of invoices of this nature, although it does not necessarily follow that this check will reveal such errors. (See **DATING FORWARD.**)

I O U.

This is a mere acknowledgment of indebtedness. There is no special form in which it is required to be made, but it should be dated, state the amount of the loan, be addressed to the creditor, and be signed by the debtor. Although, as just stated, no special form is necessary, the document is generally worded somewhat as follows—

"1st March, 19..

To James Jones.

I O U £50.

Thomas Brown."

No stamp is required. No action can be brought upon it. But it is useful as evidence of a state of indebtedness existing between Jones and Brown if the former is compelled to bring an action against the latter for the recovery of the money, and the latter denies that there is any money owing by him to Jones. But although useful as evidence of a debt existing, it does not prove the amount of the debt, as Brown may give evidence *aliunde* that he has paid off a portion or the whole of the debt.

JOBGING BOOK.

(SEE FINANCIAL HOUSES AND INVESTORS, ACCOUNTS FOR, p. 479.)

JOINT ACCOUNTS.

Joint Accounts is the name given to accounts dealing with transactions where two or more persons are concerned as principals and where an agreement exists to divide the profit on such transactions or to meet the loss concerned in portions which have been agreed upon previously. The subject-matter of joint accounts may be divided under two heads—

- (1) Joint consignments.
- (2) Joint ventures.

JOINT CONSIGNMENT.—A joint consignment is the sending of goods by a consignor to a consignee on the understanding that the consignee shall sell the goods at the best price obtainable, the price so obtained, either by public sale or by private treaty, being brought into the Joint Consignment Account. The balance on the account, after charging against the price realised, the expenses of the consignor and the consignee, and the interest involved, is divided proportionately, if a profit, or borne proportionately, if a loss, by the two or more parties concerned. It will be appreciated, therefore, that the method of keeping Joint Consignment Accounts varies from that necessary in the case of ordinary Consignment Accounts. In the case of an ordinary consignment, it is the duty of the consignee to sell the goods comprised therein at the best price obtainable. He is then entitled to deduct from the gross proceeds all the expenses to which he has been put, and also his commission, and to account to the consignor for the balance, known as the "net proceeds." The consignee, therefore, incurs no risk or liability except that which may be incurred by his own negligence. The expenses to which the consignor has been put affect him in no way, and he is not entitled to have particulars of them nor of the profit or loss resulting from the consignment, his profit being made up solely by the agreed commission which he charges by way of a percentage on the gross price realised.

In the case of a joint consignment the position is different. The relations of the parties are in the nature of a partnership, and the consignee is entitled to details of the cost price of the goods, the expense of freight, insurance, and any other charges which are to be

charged against the Joint Account and to a complete account of the result of the transaction. For his profit he must rely entirely on the result of the transaction and is not entitled, therefore, to make the percentage charge for commission as in the case of an ordinary consignment. As in the case of consignment accounts, it is necessary to have some knowledge of the procedure connected with the sending of consignments and of the method of dealing with the goods comprised in a consignment, since some knowledge of the charges which have to be paid, and of the usual procedure, is essential before a proper system of recording transactions can be put in. It is therefore assumed that study has been made of the details and principles set out in the article dealing with CONSIGNMENT ACCOUNTS appearing in this work.

JOINT CONSIGNMENT ACCOUNTS.—In order properly to record the result of a joint consignment, the duty of keeping the complete accounts relating to the transaction should be given to one of the parties concerned, and it is convenient, in order that an early settlement can be made, that the accounts should be kept by the consignee as he will be the person who will receive the amount realised by the sale of the goods comprised in the consignment.

He will open in the books a Joint Consignment Account, an account headed with the name of his partner in the joint consignment and an account headed with his own name. After the consignor has dispatched the goods he will send to the consignee an account of the charges which he has incurred and an invoice showing the cost price of the goods.

On receipt of these details the consignee will put through the books a Journal entry debiting the Joint Consignment Account with the amounts so detailed and crediting the consignor.

When the consignee takes possession of the goods by paying all charges such as freight, insurance, wharf charges, etc., he will debit up such charges to the Joint Consignment Account, crediting his own account in the books.

On the sale of the goods he will debit any further charges incurred such as brokerage, advertising and sale charges, etc., in the same way, and he will credit the Joint Consignment Account with the amount of the proceeds when he receives such amount, debiting his own account.

The sale being completed, the date to which the account is to be brought down is known.

Each of the personal accounts is ruled with an extra column on each side, in addition to the usual money columns, and interest is calculated from the date of the disbursement or from the date of the receipt in each case to the date at which the account is made up, and the amount of interest to be charged or allowed is entered in the interest column on each side. The balance of the interest columns on each account is inserted to the debit or the credit of the personal account in each case, the double entry being completed by debiting or crediting the Joint Consignment Account.

The balance of the Joint Consignment Account then represents the profit or loss on the transaction and will be transferred to the debit or credit of the personal accounts in the agreed proportions.

The Joint Consignment Account will thus close, and similar but opposite balances will remain on the personal account of each party showing the amount to be received from or paid to the other party.

In the case of a Joint Consignment Account, by whichever partner it is kept, it is in every way better to keep the accounts concerned entirely separate from the books of his general business, with a separate Cash Book and a separate Ledger. If, however, the consignee incorporates the joint accounts in his own books there will appear in his Ledger an account in the name of his partner and the Joint Consignment Account only. No account in his own name will appear. In such a case, the amount of interest to be debited or credited to the Joint Account in respect of amounts paid out or received by himself will have to be calculated and put through the Journal, the proper proportion of profit or loss affecting himself

being transferred from the Joint Account to his Trading Account or Profit and Loss Account.

In order more exactly to explain the method of treating joint consignment accounts the following example is worked out—

On 1st January, 19.., John Jones & Co., Calcutta, consigned on Joint Consignment Account to Arthur Brown & Co., London, goods to the value of £200, the arrangement being that profits or losses should be shared as to two-thirds to John Jones & Co. and as to one-third to Arthur Brown & Co., Arthur Brown & Co. to keep the Joint Consignment Account Books. On 5th January, 19.., John Jones & Co. paid the following charges, details of which they rendered to Arthur Brown & Co.—

	£	s.	d.
Packing Charges	5	10	0
Carriage	1	10	0
Insurance, Stamps, etc.	4	0	0

On 1st March Arthur Brown & Co. sold the goods through their brokers for the sum of £300, and paid the following charges—

	£	s.	d.
Insurance	2	0	0
Freight	8	0	0
Customs Entry and Stamps	10	0	
Wharfingers' Charges and Rent	7	0	0

On 15th March Arthur Brown & Co. received £296 in settlement from their brokers, being the proceeds of the sale, less brokerage £3, and sale expenses £1.

Assuming settlement at 20th March, it is required to show the Joint Consignment Account, and the accounts of John Jones & Co. and Arthur Brown & Co. in the joint consignment books.

JOINT CONSIGNMENT ACCOUNT

19..		£	s.	d.	19..		£	s.	d.
Jan. 1	To John Jones & Co., Goods	200	0	0	Mar. 15	By A. Brown & Co.	300	0	0
" 5	" John Jones & Co.—				" 20	" A. Brown & Co.—			
	Packing Charges	5	10	0		Interest		3	3
	Carriage	1	10	0					
	Insurance, Stamps, etc.	4	0	0					
Mar. 1	" A. Brown & Co.—								
	Insurance	2	0	0					
	Freights	8	0	0					
	Customs Entry Stamps		10	0					
	Wharf Charges	7	0	0					
" 15	" A. Brown & Co.—								
	Brokerage	3	0	0					
	Sale Expenses	1	0	0					
" 20	" John Jones & Co.—								
	Interest	2	5	5					
" 20	" Profit, viz.—								
	John Jones & Co. (⅔ rds.)	43	11	11					
	Arthur Brown & Co. (⅓ rd.)	21	15	11					
		£ 300	3	3			£ 300	3	3

JOHN JONES & CO., CALCUTTA

19..		Days.	Interest.			Amount.			19..	Days.	Interest.			Amount.		
			£	s.	d.	£	s.	d.			£	s.	d.	£	s.	d.
Mar. 20	To Interest Contra								Jan. 1	By Joint Consignment						
" "	" Balance carried down					256	17	4	" 5	" Joint Consignment	79	2	3	3	200	0
										Account—						
										Packing Charges	75		1	1	5	10
										Carriage	75			3	1	10
										Insurance,						
									Mar. 20	Stamps, etc.	75			10	4	0
									"	Interest					2	5
									"	Share of Profit						
										($\frac{1}{3}$ rds.)				43	11	11
			2	5	5	256	17	4				2	5	5	256	17
									19..							
									Mar. 20	By Balance brought down				£	256	17

ARTHUR BROWN & CO., LONDON

19..		Days.	Interest.		Amount.		19..		Days.	Interest.		Amount.	
			£	s. d.	£	s. d.				£	s. d.	£	s. d.
Mar. 15	To Joint Consignment A/c—Cash . . .	5		4 1	300	0 0	Mar. 1	By Joint Consignment Insurance . . .	A/c—19		1	2	0 0
" "	" " Interest . . .					3 3		Freight . . .	19		5	8	0 0
								Customs Entry and Stamps . . .	19			10	0
								Wharfingers' Charges and Rent . . .	19		4	7	0 0
							15	" Joint Consignment A/c—Brokerage . . .	5			3	0 0
								Sale Expenses . . .	5			1	0 0
							" 20	" Interest Contra . . .		3 3			
							" "	" Share of Profit (½ rd.) . . .				21	15 11
							" "	" Balance carried down . . .				256	17 4
				4 1	300	3 3					4 1	300	3 3
19..													
Mar. 20	To Balance brought down . . .			£	256	17 4							

It will be seen that the balances remaining on the accounts of the two partners are equal and opposite, representing the amount to be paid by Arthur Brown & Co. to John Jones & Co.

The above details and examples are of a Joint Consignment Account between one person who supplies the goods and another person who undertakes the sale of the goods and the management, sharing the profit or loss in agreed proportions.

Another form of joint consignment may be an arrangement between two or more persons to consign goods jointly to a consignee abroad and undertaking to share profits or losses in agreed proportions.

In such a case the consignee is an ordinary agent who charges a commission for his services in the ordinary way (see CONSIGNMENT ACCOUNTS)

and, unless some arrangement exists that he shall be one of the parties in the joint transaction, no liability attaches to him for any loss on the sale of the goods, and, conversely, he has no interest in any profit made and looks only to his commission as remuneration for his services.

In such a case also it is essential for one of the joint consignors to be made the accounting party, and he will open in the Joint Consignment Account books a Joint Consignment Account and an account for each one of the partners. Details of all accounts for goods consigned and charges paid will be given to him, and such amounts will be credited to the various partners concerned and debited to the Joint Consignment Account.

and when the amount of the net proceeds has been received, the interest on each partner's account can be calculated down to the date of settlement; such amounts will then be posted to the Joint Consignment Account, the balance of the profit or loss shown on that account then being transferred to the partners' accounts in the agreed proportions. The balances then remaining on the various partners' accounts will be found to balance in total, and the balance on each account will show the amount to be received from or paid to each partner.

The circumstances under which joint consignments may be made can, of course, be varied in many different ways, and the proportion in which the partners agree to share profits or losses varies in accordance with the risk run by each partner, or in accordance with the personal attention or management undertaken by each partner. One partner may agree to contribute the goods forming the consignment whilst another may agree to pay all disbursements connected with the transport or shipment of the goods. In circumstances where the transaction contains a large element of risk by reason of the market being an uncertain one or by reason of the goods being of a perishable nature, one of the partners may agree to contribute nothing in kind nor to contribute anything towards the expenses of the shipment, but he makes himself liable as a partner in the particular venture for a share of any loss which may have to be accounted for. In such a case he comes into the Joint Account as a speculator, relying on favourable circumstances to show a profit on the consignment. As a further example of yet another variation, one of the parties may agree to contribute a certain fixed sum which he pays over as his share in the Joint Account and on which interest is credited to him as previously explained besides the share of profit which, on a successful outcome, will become payable to him.

Whatever variations may be made in the nature of the partners' contributions, however, the principle of the keeping of the accounts follows the details given, but in all transactions, except the smallest, it is of great importance that the accounts involved should be kept entirely separate and distinct from the books of the general business of the party on whom devolves the duty of keeping the Joint Account records.

JOINT VENTURES.—Although joint consignments are very commonly known as joint ventures or joint adventures, their proper designation is joint consignments. Joint venture is the term used to imply any partnership existing between parties for the purpose of carrying out any transaction or speculation jointly on the understanding that such partnership embraces that transaction or speculation only. The partnership relation is automatically determined on the termination of

the venture, or the achievement of the object for which the partnership was created and the settlement of all accounts between the partners.

It is unusual to find any firm-name adopted by the parties carrying out the venture, since this might be held to imply a general partnership between the parties. It is usual to give the management of the venture to one of the parties and to constitute him the accounting party also, and to authorise him to enter into all necessary arrangements or contracts in his own name.

The method of keeping the accounts of a joint venture is similar to that in the case of joint consignments, the personal account of each partner being ruled with interest columns, the Joint Venture Account being debited with the expenses incurred and credited with the proceeds or profits, and the account of each partner being debited with amounts received by him or credited with payments made by him, or the agreed value of contributions by him in kind.

Examples. Cases in which joint accounts may come into operation are multifarious, but the following typical examples will explain their use.

A number of persons may undertake the flotation of a company, forming themselves into a promotion syndicate. One of the partners may undertake to put up a sum of money for the necessary cash disbursements which will have to be made and will make these advances when called upon by the accounting party. Another may undertake to carry out the necessary printing work which, in ventures of this description, is considerable. A third will undertake the payment or liability for the wide advertising necessitated and a fourth, although contributing nothing, perhaps, in cash or its equivalent, will give the benefit of his connection with financial houses or private investors for the purpose of obtaining the underwriting of, or applications for, the shares of the company to be floated. The proportion in which the resultant profit or loss will be shared will be mutually agreed between the partners of the venture according to the financial risk run by them, or according to the value of the services which will be contributed by them.

The above contributions will be dealt with as follows—

The sums in cash contributed by the first partner will be credited to his personal account and will be debited to the Joint Venture Account by way of a memorandum Cash Account, the amounts received by the accounting party being debited to such Cash Account and the payments being credited and analysed in the same way as in an ordinary analysis Cash Book under the various headings of expense. Periodically, or on the termination of the venture, the necessary Journal entry will be made passing the entries into the Joint Venture Accounts. In this way the

Joint Venture Account itself will show the headings into which the expenses are divided.

The second partner will render to the accounting party his statements of the printing carried out, or the actual invoices, the amounts of which will be credited to his account and debited to the Joint Venture Account.¹

The third partner in the same manner will advise the accounting party of the sums expended by him in advertising, or, if he be himself the advertising agent, will render to him the usual statements of advertisements inserted in papers or advertising otherwise carried out, his personal account being credited and the Joint Venture Account being debited with the charges for such advertising.

The fourth party will render his accounts for entertainment, social or other expenses incurred, and will either be credited with such expenses, the Joint Account being debited, or will draw from the accounting party the amount so expended from the fund provided by the first partner, such payments being entered in the Cash Account and finding their way to the debit of the Joint Venture Account in due course as explained above.

In due course, assuming a successful flotation, the purchase consideration will be received by the accounting party, the Joint Venture Account being credited and the account of the accounting party, whichever one of the above partners he may be, being debited. This purchase consideration received from the new company will usually be made up partly of cash and partly of shares. This must, of course, be distinguished in the necessary entries, it being remembered that no interest will be debited against the accounting party in his personal account in respect of the shares allotted forming part of the consideration money. On receipt of the purchase consideration, the interest to be debited or credited to the personal accounts of the partners and conversely to the Joint Venture Account, can be immediately calculated, and the final entry in the books will be the transfer from the Joint Venture Account to the accounts of the partners of the agreed proportions of profit. Where the purchase price received has been partly in cash and partly in shares the proportion of profit to be transferred to each partner will be made up proportionately of cash and shares unless some arrangement exists to the contrary. The transfer entry should, therefore, clearly set out the amount of each, in order that, by reference to each personal account, may be seen immediately the amount of cash to be received by or from each partner and the number of shares to be transferred to him.

As has already been shown in the example in joint consignment accounts, the debit balances on the partners' accounts will equal the credit balances unless an error exists in the books which,

if so discovered, can be readily located and corrected.

Another example of joint venture accounts quite different in character from the above is of an arrangement between a landowner or speculator and a builder, whereby the landowner brings into the venture a piece of frontage land for development by the erection of houses thereon. The builder undertakes to build the houses, but, in order to minimise his cash outlay, the landowner undertakes to provide the cash for payment of the labour as distinct from the cost of materials, administration and other expenses. It is agreed that profits or losses shall be shared or borne in equal proportions.

The necessity for separate books for the joint venture is as great here as in any other example.

The principle is the same as previously explained, the landowner being credited and the Joint Venture Account being debited with the value of the land mutually agreed between the two parties. The only special variation advisable in this case is that, instead of one Joint Venture Account, there should be one for each plot on which a house is to be erected.

The land brought into the venture will be planned out into plots and an agreed price placed upon each plot, each Joint Venture Account being debited with the value placed upon the plot to which it refers, the total being credited to the landowner partner's personal account. It must be remembered that interest will run upon this amount in favour of the landowner, being debited in due course, as already explained, to the joint venture accounts in the proper proportions, according to the time spent in developing each plot and finding a purchaser.

The builder's own accounts will be kept in the usual way, and from his books will be obtained the material for the entries affecting his personal account and the Joint Venture Account in the joint venture books.

His Materials from Stores Book and his Invoice Book will be ruled with the usual analysis columns, and a column will be provided for each of the houses to be erected in connection with the joint venture, the weekly or periodical totals being posted to the proper cost accounts in the Cost Ledger.

These figures will form the basis of the entries to be put through the joint venture books, debiting the separate joint venture accounts with the amounts of materials and crediting the builder's personal account periodically.

Although the cash outlay in respect of wages paid on the jobs will be borne by the landowner, the actual cash payments will be made by the builder in the ordinary way. His wages will be analysed in the usual way through an analysis Wages Book compiled from the workmen's time

sheets, and the amount of the wages paid out relating to the various jobs making up the venture will be ascertained from the totals of the columns applicable to those jobs at the end of each week, and a cheque in settlement of the whole amount will be given by the landowner partner to the builder. The amount of this cheque will be credited in the joint venture books to the personal account of the landowner, the various joint venture accounts being debited in the proportion shown in the builder's books.

Although the point does not affect the joint venture books, it should be remembered that in the builder's own books the debit in his Cash Book in respect of the amount of the cheque given by the landowner will be "contra" to the payments shown in his wages Analysis Book applying to the jobs in the venture, and consequently neither will require any posting to his own ledgers.

In addition to wages and materials, other cash payments will be made by the builder which may only appear in the Cash Book and which may not pass through his Invoice Book, such as surveyors', architects', and council fees, fire and employer's liability insurance, etc., and these will be posted up by him in the usual way to his cost ledger accounts. From the cost ledger accounts, therefore, should be obtained the details of amounts with which he has to be credited and the joint venture accounts debited in the joint venture books.

As regards administration charges, etc., with which the venture will have to be debited and the builder credited, these should be calculated on a percentage of the total prime cost of each job mutually agreed upon beforehand by the two partners, the basis of which will be ascertained by reference to previous periodical accounts of the builder's business.

This entry referring to administration expenses will be put through the books as each job, forming part of the venture, is completed.

As a sale of any house comprised in the venture is effected, the venture account affected will be credited, the account of the partner receiving the purchase-money being debited. The Joint Venture Account concerned will then be closed by transferring the balance to the Joint Venture General Account. As soon as the various joint venture accounts have been closed by sale of the houses and transfer of the balances to the Joint Venture General Account, the latter account can itself be completed by the calculation and posting of interest debited or credited to the partners, and by the transfer of the profit and loss shown on the account in the agreed proportions.

As a final example of an undertaking requiring joint accounts may be mentioned an arrangement between three persons, one of whom is the owner

of a patent which it is intended to exploit and place upon the market. Of the other two, one undertakes all expenses of advertising and the other all legal expenses and expenses of introductions and fees, and undertakes, further, to give his services in connection with exploiting and managing the venture, resultant profits being shared equally between the three parties.

In such a case as this it may be arranged that the patentee shall be credited with a sum representing the value placed upon the patent or representing the cost already incurred by him in expense or time before the venture was entered into and, if this is so, his personal account will be credited with such sum and the Joint Venture Account will be debited. In such a case it must be borne in mind that interest will run on the amount in favour of the patentee.

In a case of this character it is more usual to place no monetary value on the patent in the Joint Account, since it is only by the judicious expenditure of cash and the proper exploitation or introduction of the patent to persons dealing in similar articles that value in the patent is created. The patentee should look for his profit, therefore, to come only from a successful sale by the syndicate either to a private firm or to a company formed for the exploitation and sale of the particular patent or to one dealing in similar articles.

The principle in the keeping of the Joint Account is the same as in the examples given previously. Accounts will be rendered to the accounting party of sums expended in advertising, the amounts being credited to the partner concerned and debited to the Joint Venture Account.

In like manner the third party will furnish details of expenditure incurred by him which will include entertainment and introduction expenses, legal expenses and payments in respect of patent fees, etc., all of which will be credited to him, being debited to the Joint Venture Account. On the successful sale of the patent and the receipt of the purchase-money the Joint Venture Account will be credited, the interest on each of the partner's accounts will be calculated and the necessary postings made as previously explained, the Joint Venture Account then being closed by the transfer of the profit to the partners' accounts in equal proportions. The partners' accounts will then be closed by payment by the accounting party of the sums standing to their credit on the accounts.

Such an arrangement involving a patent will almost invariably be closed by sale outright of the patent rights to a person or company for the purpose of working or exploiting the patent. It can, however, easily be conceived that a satisfactory termination of the venture may not be achieved in this way, and it will be necessary for

the partners to elect whether further expense be discontinued by dropping the project, or whether the patent be worked commercially by the partners. In the former case, where it is decided to drop the project altogether, the closing date will be agreed and interest on the partners' accounts will be calculated and debited or credited to the Joint Venture Account.

The Joint Account will be closed by transferring the loss in equal proportions to the partners' accounts, and the partners' accounts will be closed by the necessary payments between the partners.

In the latter case, where it is decided to exploit the subject matter of the patent commercially, it will be impossible to continue the accounts in the form of joint accounts and the arrangement will resolve itself into an ordinary partnership, the accounts taking the ordinary form required for the particular undertaking, since it must be remembered that joint accounts come into operation only where an arrangement exists for a definite termination of the relation existing between the temporary partners when the object is achieved for which such partnership was created. (See also under PARTNERSHIP ACCOUNTS.)

JOINT ADVENTURE ACCOUNTS.

(See PARTNERSHIP ACCOUNTS, p. 766.)

JOINT CONSIGNMENT ACCOUNTS.

(See JOINT ACCOUNTS.)

JOINT CREDITOR.

When a debt is owing to two or more persons jointly, each of them is a joint creditor of the debtor.

JOINT ESTATE.

(See JOINT TENANCY, TENANCY IN COMMON.)

JOINT OWNERSHIP.

Ownership which is held by two or more persons. The most familiar instances of such ownership are joint tenancy (*q.v.*) and tenancy in common (*q.v.*).

JOINT TENANCY.

Where land is held by two or more individuals and not by one only, at the same time, and no direction has been given in the instrument creating the tenancy that the same shall be held by the beneficiaries as tenants in common, a joint tenancy is created, and the tenants have an equal interest or right in the whole of the property. The most peculiar and the most important point connected with this species of tenancy is the right of survivorship, by which the share of any deceased tenant vests in the survivors, and if there is but one survivor then in that survivor alone. A joint tenant cannot devise his interest by will,

but he can convey his share to another. This newly introduced person, however, becomes a tenant in common and not a joint tenant. Again, if one joint tenant purchases the interests of all the other joint tenants, he puts an end to the joint tenancy by reason of the sole tenancy which has become vested in him. Such a purchase is effected by a release and not by a conveyance, because each joint tenant is already equally possessed of the whole property. In order to avoid the inconvenience naturally inherent in such a holding, and especially the risk of total loss by death, if one joint tenant does not purchase the interests of the others, the proper course is for a partition suit to be instituted, when the Court will split up the estate into separate ownerships. A partition suit is always brought in the Chancery Division of the High Court, such suits having been specially assigned to it by the Judicature Act, 1873.

JOINT VENTURES.

(See JOINT ACCOUNTS; PARTNERSHIP ACCOUNTS, p. 766.)

JOURNAL, USE OF.

The Journal is a book of first entry, and, as its name implies, is a *Day Book* (French, *jour*, a day), i.e. a book in which the entries are made day by day as they take place.

In this country it is used only for the reception of items for which no special book of original entry is kept. Of these may be mentioned the opening entries of a new set of books, the closing entries at the end of each period, the appropriation of profits, those accounts of a limited company which deal with the raising of capital or debentures, and the acquirement of a business, consignment transactions and bill transactions, these latter being of so great importance that it is advisable to record them through the Journal as well as through the Bill Books, especially as the Bill Books are not recognised as part of the books of account, but only as Memoranda.

All items which require explanation, such as the writing off of bad debts, introduction of capital, and transfers from one Ledger to another, should also be passed through the Journal.

The Journal entry is made by stating the account to which the item is debited, with the amount in a first (debtor) column, and immediately beneath, the account to which the item is credited, with the amount in the second (credit) column, the total of the debit column thus agreeing with that of the credit column. Wherever necessary or advisable, a short explanation of the nature of the transaction, known as a "narration," is given under each entry.

The following are the Journal entries for a few transactions of special character, showing the

necessary narrations. Others are given under OPENING ENTRIES, CLOSING ENTRIES, and NARRATION. The Journal here given is in the ordinary form. Other forms and their uses are discussed under COLUMNAR JOURNALS and TRANSFERS.

Shipping and Bill Transactions

	£	s.	d.
Lewis & Co. buy and ship to Armstrong & Sons, of Jamaica, sundry goods invoiced as costing	1,004	11	8
The Freight, Insurance, and Dock Charges were	89	6	4
The buying and shipping commission charged was	30	2	0
Total of Invoice was	£1,124	0	0

Lewis & Co. drew on Armstrongs for that amount, and secured an advance of £650 from the bankers, through whom they were forwarding the documents.

The draft was duly accepted.

At due date of draft Armstrongs paid one-half, and gave a bill for the balance, plus 6 per cent. interest per annum for six months.

The bankers were repaid their advance by Lewis & Co., and the extended bill was met at maturity by Armstrongs.

In the Books of Lewis & Co.—

JOURNAL

	£	s.	d.	£	s.	d.
Armstrong & Sons Dr.	1,124	0	0			
To Goods Cr.				1,004	11	8
" Freight and Insurance Cr.				89	6	4
" and Dock Charges Cr.				30	2	0
" Commission Cr.						
Being cost of goods sold, and expenses in connection with shipment of same to Jamaica.						
Bills Receivable Dr.	1,124	0	0			
To Armstrong & Sons Cr.				1,124	0	0
Bill No. at m/d. due.....						
Cash Dr.	650	0	0			
To Bank Cr.				650	0	0
Advance on security of goods in transit to Armstrong & Sons.						
Cash Dr.	562	0	0			
Armstrong & Sons Dr.	562	0	0			
To Bills Receivable Cr.				1,124	0	0
Bill No. withdrawn this day on receipt of half the amount in cash.						
Armstrong & Sons Dr.	16	17	2			
To Interest Cr.				16	17	2
Interest at 6% p.a. for 6 months from date on £562, being the currency of Bill No.						
Bills Receivable Dr.	578	17	2			
To Armstrong & Sons Cr.				578	17	2
Bill No. at 6 m/d., due..... in settlement of account.						
Bank Dr.	650	0	0			
To Cash Cr.				650	0	0
Repayment of advance made to us.....						
Cash Dr.	578	17	2			
To Bills Receivable Cr.				578	17	2
Bill No. due this day duly met.						

In the Books of Armstrong & Sons—
JOURNAL

	£	s.	d.	£	s.	d.
Goods Dr.	1,124	0	0			
To Lewis & Co. Cr.				1,124	0	0
Purchase of goods as per Invoice.						
Lewis & Co. Dr.	1,124	0	0			
To Bills Payable Cr.				1,124	0	0
Bill No. at m/d. due.....						
Bills Payable Dr.	1,124	0	0			
To Lewis & Co. Cr.				562	0	0
" Bank Cr.				562	0	0
Withdrawal of Bill No.						
Interest Dr.	16	17	2			
To Lewis & Co. Cr.				16	17	2
Interest at 6% p.a. on £562 for 6 months from date, being the currency of Bill No.						
Lewis & Co. Dr.	578	17	2			
To Bills Payable Cr.				578	17	2
Bill No. at 6 m/d. due.....						
Bills Payable Dr.	578	17	2			
To Bank Cr.				578	17	2
Payment of Bill No. due this day.						

Issue of Capital and acquirement of a business by a Limited Company—
JOURNAL

	£	s.	d.	£	s.	d.
Cash Dr.	7,500	0	0			
To Application Account Cr.				7,500	0	0
Being amount of 10s. per share received on application for 15,000 shares.						
Application Account Dr.	7,500	0	0			
To Share Capital Account Cr.				7,500	0	0
Being 15,000 shares, 10s. per share paid on application, allotted as per Minute of.....						
19..						
Allotment Account Dr.	7,500	0	0			
To Share Capital Account Cr.				7,500	0	0
Being amount of 10s. per share due on allotment on 14,700 shares now received.						
Purchase of Business Account Dr.	70,000	0	0			
To Vendor Cr.				70,000	0	0
For sundry assets acquired by the Company as per agreement dated 1st January, 19.., as follows:—						
Sundry						
Debtors £20,000						
Less Reserve for Bad Debts 1,500						
				18,500		
Stock-in-Trade 10,000						
Machinery and Plant 25,000						
Loose Tools 4,000						
Bills Receivable 2,500						
Goodwill 10,000						
				£70,000		
Vendor Dr.	15,000	0	0			
To Purchase of Business A/c Cr.				15,000	0	0
For Sundry Liabilities taken over by the Company as per Agreement, dated 1st January, 19.., as follows:—						
Sundry Creditors £10,000						
Bills Payable 5,000						
				£15,000		

JOURNAL—(contd.)

		£	s.	d.	£	s.	d.
	Vendor	Dr.	55,000	0	0		
	To Ordinary Share Capital	Cr.			25,000	0	0
	" 5% Debentures	Cr.			25,000	0	0
	Being 25,000 Ordinary Shares of £1 each, and £25,000 in 5% Debentures, allotted as fully paid up, as part consideration of purchase price of business, as per agreement dated 1st Jan., 19... and Minute of.....19..						
Feb. 1	To Bank	Cr.			5,000	0	0
	Being Balance of purchase price of business as per Agreement dated 1st January, 19...						

Appropriation of the Profits of a Limited Company—
JOURNAL

		£	s.	d.	£	s.	d.
	Profit and Loss Appropriation Account	Dr.	3,750	0	0		
	To Dividends Account	Cr.			3,750	0	0
	Interim Dividend of 5% on 75,000 Shares of £1 each, paid this day as per Minute of.....						
	Profit and Loss Account	Dr.	14,060	0	0		
	To Profit and Loss Appropriation Account	Cr.			14,060	0	0
	Transfer of profit for year ended 31st March, 19..						
	Profit and Loss Appropriation Account	Dr.	2,500	0	0		
	To Reserve Fund	Cr.			2,500	0	0
	Amount placed to Reserve Fund as per Resolution passed at the Annual Meeting of Shareholders held this day.						
	Profit and Loss Appropriation Account	Dr.	7,500	0	0		
	To Dividends Account	Cr.			7,500	0	0
	Final Dividend of 10% on 75,000 Shares of £1 each as per Resolution passed at the Annual Meeting of Shareholders held this day.						
	Dividends Account	Dr.	656	5	0		
	To Income Tax Account	Cr.			656	5	0
	Tax at 1d. in the £ on the total Dividends paid during the year, deducted from the Final Dividend paid this day.						

In Continental countries whose laws are based on the Code Napoleon, the Journal is the most important book of account, and its use is strictly enforced under heavy penalties. It is the only book which will be taken as evidence in the Courts of Law, and alterations must be made in such a way that the original entry may be distinguishable and the book must be free from erasures. A Government Stamp is often impressed on each page. These legal restrictions have caused every transaction to be required to be recorded in the Journal and this fact has been the instrumental factor in delaying the development of Continental Book-keeping. (See Book-keeping.)

JUDGMENT CREDITOR.

This is a person who has instituted an action in law for a debt or for damages in contract or in tort, as the case may be, and who has obtained a judgment for the whole or a portion of the amount

claimed by him. The rights of a judgment creditor are various, but the most important are (1) power to issue execution; (2) power to issue a bankruptcy notice; and (3) power to issue a judgment summons for the committal of the judgment debtor.

JUDGMENT DEBTOR.

The person against whom a judgment has been obtained in an action at law, ordering him to pay a certain sum of money, such order not having been satisfied. A judgment creditor is entitled to issue execution against the judgment debtor, and if this is not successful he may institute bankruptcy proceedings to this extent, that is, he can serve a bankruptcy notice upon him. If this bankruptcy notice is not satisfied, the judgment creditor may then go further and ask for a receiving order. Another method of seeking satisfaction against a judgment debtor is for the judgment creditor to have him brought before the Court on a judgment summons, and if it is then proved to the satisfaction of the Court that the debtor has had the means of paying the judgment debt since it was incurred and has failed to do so, an order may be made committing him to prison.

JUDICIAL TRUSTEE ACT, 1896.

Under this Act the legislature provided for the appointment of an official who was to be known as a "judicial trustee." By the provisions of the Act, a judge of the High Court, or, in certain cases, the judge of a County Court, is empowered, upon application being made by the creditor of a trust, or by the trustee or beneficiary under an existing trust, to appoint any fit or proper person who has been nominated for the purpose as a judicial trustee. This person so nominated is then empowered to act either alone or in conjunction with some other person in the administration of the trust. In special cases, provided sufficient cause is shown, a judicial trustee may be appointed to take the place of an existing trustee or of existing trustees. The Act provides for a certain remuneration being paid to the judicial trustee, who is also compelled to render periodical accounts of his trusteeship in a prescribed manner. For these particulars the Act must be consulted. In all probability the Act will become, if it has not already become, a dead letter, owing to the passing of the Act which set up the office of the public trustee in 1906.

JURAT.

From the Latin, *juratus*, sworn. This is the clause written at the foot of a deed or affidavit, stating when, where, and before whom the document was sworn.

JUS DISPONENDI.

The right of disposing of property.

KEEPING HOUSE.

ONE of the acts of bankruptcy mentioned in the Bankruptcy Act, 1914, is that of "keeping house." It is not possible to give an exact definition of this expression in a short form, but its meaning is fairly clear, and arises in this way. In order that a bankruptcy petition may be presented against any individual, it is necessary that certain preliminary proceedings should be taken, and to enable these proceedings to be carried out, personal service upon the debtor is requisite. The debtor, however, may endeavour to keep out of the way, and he might conceivably outwit his creditors altogether if something in the shape of substituted service was not provided. It is, therefore, enacted by Section 1 of the Act of 1914, that "If, with intent to defeat or delay his creditors, he (*i.e.* the debtor) does any of the following things—namely, departs out of England; or being out of England remains out

of England; or departs from his dwelling-house; or otherwise absents himself; or begins to keep house," he commits an act of bankruptcy, and proceedings against him may be taken forthwith. The gist of "keeping house" is the wilful avoidance of an interview with another person. It is sufficient to show that a debtor has given orders that he was to be denied to his creditors and other persons, and that a creditor was, in fact, so denied. But a creditor could not assert that he was denied if the debtor refused to see him at an unreasonable hour. If, however, it is clear under all the circumstances that there is an intention to avoid creditors, the act of bankruptcy is committed.

KINTLEDGE or KENTLEDGE.

The name given to the ballast of a ship, generally consisting of some heavy material, which is considered to be a part of the ship itself.

LAND AND BUILDINGS.

So far as is possible, these two assets should be recorded in separate accounts. The accounts should be charged with the actual cost of acquiring the assets and may include the legal expenses incidental to the transfer of the property.

In the case of land, the auditor should verify its existence as an asset belonging to the business, and its cost, by reference to the title deeds, and to the solicitor's bill of costs. In the case of buildings acquired by purchase the title deeds should be examined, and the Apportionment Account should be inspected to see that the charges accrued due or paid in advance, which are included in that account, have been carried to the appropriate nominal accounts and that only the actual purchase price, plus legal charges, has been debited to Buildings Account.

In the case of buildings constructed by the business, the builders' contracts and day bills, and architects' certificates, should be produced in support of the expenditure debited to the account.

The auditor must also see that an adequate provision for depreciation is made from time to time, so that these assets shall appear in the Balance Sheet at a value approximating to their worth to the business as a going concern. (See also ACCOUNTS, CRITICISM OF, p. 18; BOOK VALUES.)

LAND CHARGES.

These are any charges or rights which are secured in such a manner as to entitle a creditor to obtain satisfaction for his debt out of the lands of the debtor if the same was not liquidated in some other manner. The most common examples of land charges—apart from mortgages, which are in a different category—are writs of *elegit* (*q.v.*) and the rights of a receiver in possession.

LAND CHARGES ACT, 1888.

Prior to the passing of this Act, when proceedings were taken under a writ of *elegit* (*q.v.*) or when a receiver was appointed, there was no necessity for anything to be done on the land itself nor for any registration to be made. Consequently, an intending purchaser of land had no means of ascertaining whether land had been delivered in execution, and he ran the risk when purchasing the property, and after the payment of the purchase money, of finding that some creditor had a prior claim to himself. This did actually happen in one case, and it was held that the purchaser, in spite of the fact that he had acquired the legal estate, was postponed to the creditor. It was to avoid a repetition of this

state of affairs that the Land Charges Act, 1888, was passed. This Act provides, by Sections 5 and 6—

5. (1) There shall be established and kept at the office of Land Registry a register of writs and orders affecting land, and there may be registered therein, in the prescribed manner, any writ or order affecting land issued or made by any Court for the purpose of enforcing a judgment, statute, or recognisance, and any order appointing a receiver or sequestrator of land.

(2) Every entry made in pursuance of this section shall be made in the name of the person whose land is affected by the writ or order registered.

(3) The registration of a writ or order in pursuance of this Act shall cease to have effect at the expiration of five years from the date of the registration, but may be renewed from time to time, and, if renewed, shall have effect for five years from the date of the renewal.

(4) Registration of a writ or order in pursuance of this section shall have the same effect as, and make unnecessary, registration thereof in the Central Office of the Supreme Court of Judicature in pursuance of any other Act.

6. Every such writ and order as is mentioned in section five and every delivery in execution or other proceeding taken in pursuance of any such writ or order, or in obedience thereto, shall be void as against a purchaser for value of the land unless the writ or order is for the time being registered in pursuance of this Act.

Provided that—

(a) Where the writ or order is at the commencement of this Act registered in pursuance of the Act of the session held in the twenty-seventh and twenty-eighth years of Her Majesty, chapter one hundred and twelve, intituled "An Act to amend the law relating to future judgments, statutes, and recognisances," nothing in this section shall affect the operation of such writ or order until the expiry of the period for which it is so registered.

(b) Where the proceeding in which the writ or order was issued or made is for the time being registered as a *lis pendens* in the name of the person whose land is affected by the writ or order, nothing in this section shall affect the operation of such registration.

Proviso (a) of Section 6 has been repealed by the Land Charges Act, 1900, and by Section 3 of this last mentioned statute it is provided that Section 6 of the Act of 1888 "shall apply to every writ and

order affecting land issued or made by any Court for the purpose of enforcing a judgment, whether obtained on behalf of the Crown or otherwise, and whether obtained before or after the commencement of the Act, and to every delivery in execution or other proceeding taken in pursuance of any such writ or order, or in obedience thereto."

The Act makes no change in the law as between the execution creditor on the one hand and the execution debtor, or volunteers claiming under him, or other execution creditors on the other hand. It only affects the position of the execution creditor and purchasers for value (including mortgagees) claiming under the execution debtor. If the rights of the execution creditor are to prevail over those of a purchaser for value, it is essential that both delivery in execution and registration of the writ, or other process of execution, should take place before the completion of the purchase.

It is for these reasons that it is always most important that intending purchasers of real property should search the register to see whether there are any charges outstanding against the estate before the completion of the purchase. If they neglect to do so, they may find themselves in the long run in legal possession of an estate saddled with heavy charges, and may be without any advantageous pecuniary remedy against the vendor.

LAND COMPANY, AUDITORS AND.

(See AUDITING, p. 77.)

LAND, FREEHOLD AND LEASEHOLD PREMISES.

(See RENEWALS and DEPRECIATION.)

LAND TRANSFER ACT, 1897.

This was the Act which made an important change in the devolution of an estate on the death of the tenant. Under it the real estate (excluding copyholds) of a deceased person vests in the executor or the administrator, instead of vesting at once, as was formerly the case, in the devisee or the heir-at-law. The statute, however, makes no alteration in the law as to the ultimate right of the heir in the case of intestacy, but the personal representative of the deceased, executor or administrator, holds it in trust for the person or persons entitled to it, and he or they may require the transfer of the real property to them as they had previously a right to the personal property. As a result of the passing of the Act, probate and administration are now granted in respect of real estate, even when there is no personal estate at all.

In the administration of the estate of a deceased person, the realty is now liable, in the hands of the personal representative, for the debts of the deceased, whether expressly charged or not. The personal representative is also empowered to deal with the realty by way of sale, mortgage, or

otherwise in order to satisfy the claims which are legally made. But this liability has not altered the order of administration in any particular. The residuary personal estate is that which is primarily liable, and no recourse can be had to the realty until the whole of the personalty has been exhausted.

The Land Transfer Act, 1897, had also another object in view, namely, the compulsory registration of land. In this respect, however, it has not been altogether successful, as the provisions relating to registration are optional. No land in any county is affected unless an order in Council has been made to that effect. This portion of the Act is now in operation in the whole of the county of London. All ordinary sales of freeholds, all sales of leaseholds having forty or more years still to run, or two or more lives still to fall in, and grants of leases or underleases for the same periods are to be registered. But registration does not apply to a lease created for mortgage purposes, or containing an absolute prohibition against alienation.

The procedure on registration is as follows. The applicant or his solicitor attends the registry with the deeds relating to the property, and a copy of the same, written on stout paper, for filing. A plan must also be produced. The land is identified on a large scale ordnance map kept at the registry, and the draft entries for the register are prepared and settled. A land certificate is then drawn up and forwarded to the applicant or his solicitor. The register is private, and no examination can be made except with the authority of the registered owner, or on notice to him.

Full particulars may be obtained as to registration, at the offices of the Land Registry, Lincoln's Inn Fields. As is well known, registration is compulsory under other Acts in Middlesex and Yorkshire.

LANDED PROPRIETORS, AUDITORS AND.

(See AUDITING, p. 114.)

LANDLORD IN BANKRUPTCY, POSITION OF.

(See BANKRUPTCY: LANDLORD, POSITION OF.)

LAPSE.

This is the falling of a legacy into the residue by reason of the death of the legatee during the testator's lifetime. An exception to this is that where a child of the testator pre-deceases him and leaves issue, the legacy does not lapse, but is payable as though such child died immediately after the testator. (See also EXECUTORSHIP ACCOUNTS.)

LARCENY.

The legal name applied to what is commonly known as theft. It consists in the stealing, taking,

and carrying away of any article which is capable of being stolen out of the possession of another person with the intention of depriving him permanently of the possession of the same. It will be noticed that the word "possession" is here used, for it is larceny to steal, take, and carry away an article from a person who has the possession but who may not have the actual property in the same. Thus, A has a watch which he lends to B. It is larceny on the part of C, if C takes it from B, and B can prosecute C for the felony just as A could have done if it had been taken out of the possession of A. It is the custom in an indictment to charge an offender not only with the larceny of the goods the subject-matter of the charge, but also with "receiving the same well knowing them to have been stolen." So that even though the direct taking cannot be proved, if the person charged is found in possession of stolen goods, he must give a satisfactory explanation of how he came into possession of the same, otherwise he is equally guilty of larceny. If goods are taken for a mere temporary use, this is not larceny, but the burden of proving that there was no felonious intent is upon the person charged.

LAW COSTS IN BANKRUPTCY.

(See BANKRUPTCY ACCOUNTS, p. 208; LEGAL EXPENSES.)

LAW MERCHANT.

Law merchant, mercantile law, or *lex mercatoria*—all meaning the same thing—is, in a general sense, that body of usages and customs recognised amongst merchants and gradually incorporated in and added to the common law of the realm. In the early stages of our history it was exceedingly difficult to induce the courts to take any notice of the customary rules which obtained amongst merchants and traders in carrying out their numerous transactions; but the strong antipathy at one time felt towards these usages and customs was eventually conquered, owing mainly to the efforts of Lord Holt and Lord Chief Justice Mansfield in the seventeenth and the eighteenth centuries respectively. These customs and usages were derived from numerous sources, but more especially from the Roman Law and from the codes of the various maritime states which flourished at different periods.

It was only by very slow degrees, however, that this so-called mercantile law made its way in this country in the first instance; but now it seems that when once a general usage or custom has been judicially ascertained and established, it becomes a part of the law of the land, and the courts of justice are bound to know it and to recognise it as such. The law in connection with certain branches of commerce has been drawn up in specially codified statutes in quite recent times, and no doubt this process of codification will

make great progress. Examples of recent codification are the Bills of Exchange Act, 1882; the Factors Act, 1889; the Sale of Goods Act, 1893; the Merchant Shipping Act, 1894; the Companies (Consolidation) Act, 1908; the Bankruptcy Act, 1914; and the Deeds of Arrangement Act, 1914.

No better account of the law merchant has ever been given judicially than in the following words, taken from the judgment of Lord Chief Justice Cockburn, in the case of *Goodwin v. Roberts*, 1875, 10 Ex. 307—

"The law merchant is sometimes spoken of as a fixed body of law, forming part of the common law, and, as it were, coeval with it. But, as a matter of legal history, this view is altogether incorrect. The law merchant thus spoken of with reference to bills of exchange and other negotiable securities, though forming part of the general body of the *lex mercatoria*, is of comparatively modern origin. It is neither more nor less than the usages of merchants and traders in the different departments of trade, ratified by the decisions of courts of law, which, upon such usages being proved before them, have adopted them as settled law with a view to the interests of trade and the public convenience, the court proceeding herein on the well-known principle of law that, with reference to transactions in the different departments of trade, courts of law, in giving effect to the contracts and dealings of the parties, will assume that the latter have dealt with one another on the footing of any custom or usage prevailing generally in the particular department. By this process, what before was usage only, unsanctioned by legal decision, has become engrafted upon, or incorporated into, the common law, and may thus be said to form part of it."

LEASE.

A lease is a conveyance of lands or tenements to a person for life, or for a term of years, or at will, in consideration usually of a return of rent or some other recompense. The person who so conveys the lands or tenements is called the lessor; the person to whom they are conveyed is called the lessee; and when a lessor so conveys lands or tenements to a lessee he is said to lease, to demise, or to let them. In reality, the term lease is the same as the term tenancy, but it has now become customary to speak of the relationship of landlord and tenant, that is, of lessor and lessee, under the former designation when the term for which the lands or tenements are demised is more than three years. In the main, however, the incidents attaching to a lease and an agreement for a tenancy are the same.

Until the passing of the Statute of Frauds, all leases and agreements as to tenancies could

be made by word of mouth. And this is still the case when a lease does not exceed three years from the making, and the rent reserved is at least two-thirds of the improved value of the premises. All other leases, however, were required by the Statute of Frauds to be in writing, and since 1845 all leases which are required to be in writing must be made by deed. But if the tenant does not go into possession at once there must still be some agreement in writing as to the tenancy, in order to satisfy the fourth section of the Statute of Frauds as to an interest in land. For example, if a tenant agrees to take a house for any period, commencing next week, and there is no evidence of the same in writing, he will have no right of action against the landlord if the latter refuses to admit him. But if the tenant once gets into possession the parol agreement is quite enough for all purposes, except that if the verbal agreement was for a period beyond three years or at a rent not equal to two-thirds of the improved value, the lease is void but there is a tenancy at will, which will be converted into a tenancy from year to year when the tenant has once paid an instalment of rent.

Since the Judicature Act an agreement for a lease (being properly stamped as a lease) is just as effectual as a deed, if the tenant has gone into possession. "A tenant holding under an agreement for a lease, of which specific performance would be decreed, stands in the same position as to liability as if the lease had been executed. He is not, since the Judicature Act, a tenant from year to year; he holds under the agreement, and every branch of the court must now give him the same rights. There is an agreement for a lease under which possession has been given. Now, since the Judicature Act, the possession is held under the agreement. There are not two estates as there were formerly, one estate at common law by reason of the payment of the rent from year to year, and an estate in equity under the agreement. There is only one court, and the equity rules prevail in it. The tenant holds under an agreement for a lease. He holds, therefore, under the same terms in equity as if a lease had been granted, it being a case in which both parties admit that relief is capable of being given by specific performance."

The lessor may be the tenant in fee simple, the tenant in tail, or the tenant for life of the lands or tenements leased, although there are special restrictions, under the Settled Land Act, 1882, as to the period for which the second and the third of these may grant leases. Again, a mortgagor or a mortgagee in possession, unless restrained by the mortgage deed, may grant leases of a certain duration. In other cases, the mortgagor and the mortgagee must concur in making a valid lease. An executor may make a valid lease even before he

has obtained a grant of probate. Lastly, a copyholder may also grant a lease, but such lease must not exceed one year in duration without the consent of the lord of the manor, otherwise there is a ground for forfeiture.

The contents of a lease must depend upon the nature of the property, and all the terms must be carefully drafted. Nothing must be left to chance, and as this is essentially the work of the experienced conveyancer, it must be left to him to express the intentions of the parties to the contract. Except in so far as any of the ordinary rules attaching to the relationship of landlord and tenant are expressly excluded, the same are incorporated in every lease.

As to the stamp duties payable upon leases, see **STAMP DUTIES**.

LEASEHOLD.

This is the name which is applied to lands or tenements held under a lease for a fixed period or a definite number of years. The terms of the holding are set out in the lease or agreement which constitutes the contract between the landlord and the tenant, and, without going into particulars, it is enough to say that the covenants imposed upon the tenant are four in number: (1) To pay rent; (2) To pay rates and taxes on the property, except the landlord's property tax and the tithe rent charge (if any); (3) To keep and deliver up the premises in repair; and (4) To permit the lessor to enter at intervals for the purpose of inspecting the state of repair. In addition to any express covenants, the lessor undertakes to let the lessee have uninterrupted and quiet enjoyment of the property as far as he is concerned.

Leaseholds are always personal property, irrespective of the length of the terms for which they are made.

LEASEHOLD LAND AND BUILDINGS.

(See **BALANCE SHEET**, p. 144.)

LEASEHOLD PROPERTY, AUDITORS AND.

(See **AUDITING**, p. 92.)

LEASEHOLD PROPERTY, DEPRECIATION OF.

(See **DEPRECIATION**, p. 411.)

LEASEHOLDS RESERVE.

(See **BALANCE SHEET**, p. 142.)

LEDGER.

This is the principal book of account, and in it the items are classified under the various headings to which they belong, accounts being kept for persons from whom goods are purchased, persons to whom goods are sold, the various expenser incurred in conducting the business, the goods

where the Ledgers are self-balancing, but also the adjustment of the accounts, the transference of accounts to others where necessary, their ruling off, and the carrying down of the remaining balances. It is a term which is applied in particular to the closing of the Ledgers at the termination of each financial period.

Assuming all postings are made and the Trial Balance agreed, the work is as follows—

DEBIT LEDGER.—Stocktaking Statements, with a request that they shall be checked by the customer and returned, are sent out, and on their being received from the debtors duly certified as correct or otherwise, any differences are gone into and the accounts adjusted. Any bad debts are then written off, and the balances considered for the purpose of creating reserves for discounts and doubtful debts.

CREDIT LEDGER.—Statements to date are obtained from all creditors, and differences being settled, the accounts are adjusted accordingly, and consideration given to the reserves for discounts it is expected will be received on payment.

It is customary with some firms to bring down the balances in the Debit and Credit Ledgers. This is an excellent practice, and, especially when these are brought down in red ink, affords a means whereby their abstraction is easily done.

NOMINAL AND PRIVATE LEDGERS.—All postings should be carefully scrutinised, especially as regards the correctness of allocations made between capital and revenue, and of these the following should be specially considered, with a view to the ascertainment of the amount to be written off—

(a) Expenditure, part of which increases the value of the asset, but part of which is undoubtedly an expense.

(b) Expenditure benefiting revenue for a longer period than that under review, and hence distributed over future operations, as advertising on a specially large scale, or travelling expenses opening up new ground.

Charges incurred in acquiring or improving assets, as those on

- (1) The purchase of land or buildings;
- (2) Expenses of development of patents and patent fees;
- (3) Expenses of flotation of a limited company, or of issuing new stock, shares, or debentures; should be allocated to their respective accounts, these all being capital expenditure.

The "Apportionments" will next be given attention, and all items which are accruing, but not yet due, will be computed for the period they have run since the commencing date of the account, the amount debited to the old account, and carried down to the credit of the new period. Of these may be mentioned such items as rent, rates, gas,

electricity, wages, salaries, commissions payable and receivable, interest, rebates on bills, dividends, etc.

The following example shows the method of working, assuming that the balancing was being done to 31st August, although the apportionments are often taken at a round figure—

Rent, £200 per annum.

24th June—31st August = 68 days

$\frac{68}{365} \times £200 = £37 \text{ 5s. 2d.}$

In the same way, expenses paid, which have not expired, will have to be dealt with, their entry through the accounts being, of course, the reverse of the foregoing. Of these there is always an unexpired apportionment on account of insurance, and often an unexpired amount on rates. This last item deserves special mention, it being a common custom to pay by instalments, and hence the apportionment for the portion of the *municipal year* in this case must be made, the balance between this and the amount paid on account being the proportion due or unexpired at the date of balancing.

A Nominal Ledger Account when adjusted and balanced will appear as follows—

Dr.		RENT, RATES, LIGHT AND INSURANCE.								Cr.			
19..				£	s.	d.	19..				£	s.	d.
Aug. 31	To B/d.		398	4	10		Aug. 31	By Insurance unexpired		15	2	6	
"	" Rent accrued		37	5	2		"	" Transfer to Profit and Loss A/c		432	17	4	
"	" Rates accrued		12	9	10								
			£447	19	10					£447	19	10	
Sept. 1	To Insurance unexpired b/d.		15	2	6		Sept. 1	By Rent and Rates accrued b/d.		49	15	0	

The Discounts Accounts will be adjusted by the reserves on debtors and creditors already mentioned.

Finally, the assets must be considered individually and adequate depreciations made, stock taken, Trading and Profit and Loss Accounts drawn, reserves for bad debts, or for contingent or other purposes, created; and the Balance Sheet prepared.

LEDGER, SUNDRIES.

(See SUNDRIES LEDGER.)

LEDGER, TABULAR.

(See TABULAR LEDGER.)

LEDGERS, CARD.

(See CARD LEDGERS.)

LEDGERS, LOOSE-LEAF.

(See LOOSE-LEAF LEDGERS.)

LEDGERS, SECTIONAL.

(See SECTIONAL LEDGERS.)

LEDGERS, SELF-BALANCING.

(See SELF-BALANCING LEDGERS.)

LEGACIES.

A gift of personality by will is known as a *legacy*, whilst gifts of real property are called *devises*. Legacies are of four kinds: specific, demonstrative, general, and residuary. A *specific* legacy is a gift of a particular thing in the testator's possession (e.g. "the oil painting by Van Dyck"); a *demonstrative* legacy is partly specific and partly general (e.g. "£100 from my deposit account at the — Bank"); a *general* legacy is a gift of money without the indication of a specific fund or a gift of goods, whether in possession of the testator or not (e.g. "£100 to my valet," "a diamond pin to my secretary," etc.); a *residuary* legacy is the gift of the balance of personal estate or a part of the balance after debts and particular legacies have been paid; such gifts are in a sense specific.

If during his life the testator has disposed of the subject-matter of a specific legacy, the gift fails and is said to be *adeemed*; but if the fund from which a demonstrative legacy is given will not meet the charge, it is paid out of the general estate.

The payment of debts precedes the payment of legacies; and in the case of assets being insufficient to pay debts without encroachment on assets particularly bequeathed, legacies abate. General legacies are affected first rateably amongst themselves, then specific legacies. Demonstrative abate with specific if the fund from which they are payable exists, but with general legacies if the fund is not in existence at the testator's death. Legacies, although given by will, vest only when the executor *assents* after deciding that the assets are sufficient.

DONATIO MORTIS CAUSÂ.—A *donatio mortis causâ* is a gift made personally by the donor on the understanding that it takes effect if the donor dies of an existing sickness. It is made by delivery or placing the donee in possession of the property either actually or constructively—e.g. by giving directions as to place of rest of chattels and handing over the means of taking possession (key of a chest).

The donor's cheque, a lease, title deeds cannot be subject of such gift; but a third party's cheque, bill, or note may.

No assent of the executor is required in case of a *donatio mortis causâ*, but such a gift is liable to abatement on insufficiency of assets, and estate and legacy duty are payable in respect of it.

VESTED AND CONTINGENT GIFTS.—The gift of property to a beneficiary under a will may be dependent on the happening of a given event (e.g. "To X when he shall attain the age of 21 years"). Such a gift is said to be contingent. If, however, interest is to be paid to X until he attains 21, the gift is vested, but payable in future.

A vested legacy is one payable immediately, but it cannot be enforced until the executor is satisfied that the subject-matter will not be

required to meet liabilities. To settle up affairs, the executor has a year, called the "executor's year," at the end of which the legacy can be claimed with interest at 4 per cent. from such time. The executor's year does not affect creditor's right to sue. (See also EXECUTORSHIP ACCOUNTS, p. 462.)

LEGACY DUTY.

(See EXECUTORSHIP ACCOUNTS, p. 454.)

LEGAL ASSETS.

The assets which, in action at common law, may be made available by the creditors to meet their claims against the estate of a deceased person, and comprise all the personality of the deceased, any debts due to him, and all other property devolving upon his legal personal representative. The debts are payable in a certain order out of the legal assets marshalled in a certain order.

LEGAL ESTATE.

When the actual personal title to land is complete, the person who has such a title is said to have the legal estate, and he is in such a position towards the same that he can deal with it as he chooses. The legal estate is used in contradistinction to the equitable estate, which is what a person is said to have when, in spite of the fact that he enjoys the profits and benefits arising out of the estate, he is unable to deal with it on his own account.

LEGAL EXPENSES

Legal expenses incurred in connection with the purchase of land and buildings and the acquirement of other permanent assets may reasonably be regarded as part of the cost of such assets, and may consequently be capitalised.

Legal expenses incurred in connection with the flotation of a company and the preparation of its Memorandum and Articles of Association are usually included amongst preliminary expenses, and are, therefore, temporarily capitalised. This item should, however, be completely written off within a period of three or four years.

Legal expenses incurred in connection with the raising of capital, loans and mortgages, and the maintenance of the validity of patent rights, are sometimes temporarily capitalised in the same way as the legal expenses of flotation; but the auditor should oppose this practice, and require that expenses of this nature shall be provided out of revenue forthwith, since the sum so expended produces no tangible asset.

Legal expenses incurred in the recovery of debts and in all trading matters are proper revenue charges, and the auditor should see that they are so charged.

Legal expenses and costs in connection with suits, and arbitrations in which judgments and

awards have not been made, constitute contingent liabilities, and it is the duty of the auditor to see that a memorandum is made of such contingent liabilities at the foot of the balance sheet.

It is not uncommon for accruing legal charges to be overlooked when the accounts are being prepared, owing to the solicitor's account not having been rendered. The auditor should, therefore, be alive as to this possibility, and request that inquiry be made for any outstanding charges on this account, and see that the accrued liability is included in the Balance Sheet.

LEGAL MORTGAGE.

There are two kinds of mortgages, legal and equitable. The former arises when the mortgagor conveys the property mortgaged by deed to the mortgagee; the latter is when the mortgagor deposits the title deeds referring to the property mortgaged without any deed being executed, whether there is any accompanying note or memorandum of charge or not. (See MORTGAGE.)

LEGAL PERSONAL REPRESENTATIVE.

The person in whom the estate of deceased becomes vested, *i.e.* the executor, administrator, or trustee. (See also EXECUTORS AND ADMINISTRATORS; EXECUTORSHIP ACCOUNTS, p. 449.)

LEGAL TENDER.

This refers to the tender of money of such a kind that the creditor is legally bound to accept in discharge of a debt. To be in order a tender must be of the exact amount without necessitating any change being given. By the Coinage Act of 1870 the following are declared to be legal tender—

Gold coins to any amount,

Silver coins to an amount not exceeding 40s.,

Bronze coins to an amount not exceeding 1s.

Pre-Victorian gold coins are not now legal tender, as they were called in by the Coinage Act, 1889. Bank of England notes are legal tender in England for sums over £5, and, although they circulate freely in Scotland and Ireland, they are not legal tender in these countries if objected to by the person to whom they are being paid. In the Isle of Man and in the Channel Islands, notes are not legal tender. Scotch notes are not legal tender in Scotland, nor are Irish notes legal tender in Ireland, except Bank of Ireland notes when used in payment of the Revenue of Ireland. The £1 and 10s. currency notes issued by the Treasury shortly after the outbreak of war with Germany in 1914 are legal tender in the United Kingdom to any amount.

LETTER OF ALLOTMENT.

(See ALLOTMENT, LETTER OF.)

LETTER OF REGRET.

(See REGRET, LETTER OF.)

LETTERS OF ADMINISTRATION.

(See EXECUTORSHIP ACCOUNTS, p. 448.)

LEX NON SCRIPTA.

The unwritten law. This does not refer to that negation of law which has been so frequently spoken of in quite recent times in connection with certain offences of a criminal character, but that part of the law which is not set out in statutes, rules, and orders, and which has arisen out of custom or out of the decisions of judges in special cases. The common law of England is unwritten law except in so far as it has been modified and altered by statute.

LIABILITIES.

Amounts which a person or group of persons owes another. (See also ACCOUNTS, CRITICISM OF, p. 19.)

LIABILITIES AND ASSETS ACCOUNT.

(See AUDITING, p. 104.)

LIABILITIES, CONTINGENT.

(See CONTINGENT LIABILITY.)

LIABILITIES, GROSS.

(See BANKRUPTCY ACCOUNTS, p. 159.)

LIABILITIES TO OUTSIDERS.

(See BALANCE SHEET, p. 136.)

LIABILITIES TO OWNERS OF BUSINESS.

(See BALANCE SHEET, p. 140.)

LIABILITY OF MEMBERS OF LIMITED COMPANY.

(See MEMORANDUM OF ASSOCIATION.)

LICENCE.

An authority granted by one person to another, under which the latter is permitted to do certain things which would otherwise be held to be illegal. Thus, if A is the owner of an estate, he is, generally speaking, entitled to exclude all persons from trespassing upon his land. But if he grants express permission to B to go in and upon the land, B is said to possess a licence, and what would otherwise be a trespass is turned into a right. At one time it was held that a licence of this kind, even though under seal, was revocable by the licensor. The leading case on the subject is *Wood v. Leadbitter*, 1845, 13 W. & M. 838. This is no longer the rule. It is quite true that a mere voluntary licence may be revoked at any time; but if the licence is given for any valuable consideration—or under a deed—there is an authority coupled with an interest, and any breach of the terms of the authority, as, for example, by revocation contrary to the conditions thereof, would give the licensee a right of action for damages.

LIEN.

This is a term which signifies the right of a person to retain possession of the goods of another until some debt or obligation which has been created between the parties has been discharged. There are three kinds of lien, (a) possessory, (b) maritime, and (c) equitable. In any case lien cannot arise unless the goods over which the same is claimed have come lawfully into the possession of the person who retains them.

A possessory lien may be either particular or general. As to the former it most frequently arises in cases like the following, namely, where goods are delivered to a carrier and the consignee refuses payment. The carrier cannot be compelled to give up the goods until his charges have been paid. Again, an innkeeper is entitled to retain the goods of a guest who comes to his house if the guest refuses to pay his bill. But the most common example is that of a tradesman or a labourer who has had goods confided to his care for the purpose of doing some work upon them and who cannot be compelled to deliver up the goods until he has received the recompense stipulated for.

A general lien is one that arises either from custom or contract. It is the right to retain goods not only in respect of a debt incurred in connection with them, but also in respect of a general balance of account between the owner and the possessor. Common examples of general lien are those of factors, bankers, auctioneers, stock-brokers, wharfingers, and, in some instances, insurance brokers.

A possessory lien, whether particular or general, does not, unless there is some agreement or contract to the contrary, bestow upon the possessor the right of sale. There are, however, certain statutes which have made an exception to this rule, especially in the case of an innkeeper and a wharfinger. The lien is naturally extinguished if there is a surrender of possession to the owner, and there are various other methods in which the right can be brought to an end. Whether the right has or has not been lost is often a question of fact depending upon the special circumstances of the case.

A maritime lien is a peculiar right which attaches to a ship, wherever it may be, in respect of advances made for the prosecution of its voyage or for supplying necessities. The right is, of course, independent of possession, and if the various charges owing in respect of it are not paid, it is enforceable by arrest and sale, such arrest and sale being made at the instance of the Admiralty Court, if necessary.

Maritime lien also attaches in cases of salvage, bottomry bonds, seamen's wages, and payments for the services of pilots.

An equitable lien is one which is altogether

independent of possession, being a right to demand that a particular portion of property shall be dealt with in a particular way for the satisfaction of specific claims.

LIFE INTEREST.

The beneficial interest enjoyed by a person in property during the lifetime of a specified individual, either his own or that of some other person. If a person has an estate only so long as another person lives, it is said to be an estate *pur autre vie*. No one who has but a life interest can deal with the property beyond the extent of that interest, except under the special powers granted by and in accordance with the various Settled Land Acts.

LIFE POLICY IN PAYMENT OF DEBT.

The premiums paid upon the life policy held in these circumstances must be debited to a "Policy Account." The balance on this account must be maintained at the surrender value of the policy. Any balance in excess of the surrender value must be written off to Profit and Loss Account. If the debt is to be redeemed out of revenue, a sum equal to the amount added to the Policy Account from time to time must be charged against the Profit and Loss Account and credited to a Redemption Fund. When the policy matures, the excess of the sum receivable over the surrender value of the policy shown by the account must be debited to the Policy Account and credited to the Redemption Fund, which then becomes a reserve.

In this connection the auditor should verify the premiums paid by an examination of the policy and the premium receipts. He should require the production periodically of a certificate from the insurance company stating the surrender value of the policy at the date of making up the books, and should insist that the policy must not stand at a sum in excess of this valuation.

LIFE TENANT.

The person who is entitled to the income from settled property. (See also EXECUTORSHIP ACCOUNTS, p. 470.)

LIGHTING.

(See AUDITING, p. 81.)

LIMITATION OF ACTIONS.

There is a maxim which says that it is for the benefit of the State that there should be some limit imposed upon litigation—*Interest reipublicae ut finis sit litium*. In accordance with this maxim, certain statutes have been passed at various times, known as Statutes of Limitation. The first of these is the statute of James I, in 1623, which refers in the main to actions in contracts and tort. This statute is referred to more particularly under the heading of STATUTE-BARRED DEBTS. The second is that of William IV, in 1833. This

statute is mainly concerned with rights affecting real property, especially those known as easements, and the time fixed for bringing any action in respect of these is twenty years, with the usual extension allowed in cases of infancy and insanity. The third statute is the Real Property Limitations Act, 1874. By Section 1 of this Act it is provided: "After the commencement of this Act no person shall make an entry or distress, or bring an action or suit, to recover any land or rent, but within twelve years next after the time at which the right to make such entry or distress, or to bring such action or suit, shall have first accrued to some person through whom he claims; or if such right shall not have accrued to any person through whom he claims, then within twelve years next after the time at which the right to make such entry or distress, or to bring such action or suit, shall have first accrued to the person making or bringing the same." This time may be extended in the case of disabilities arising from infancy, lunacy, or absence beyond the seas, as in the case of contracts; but the utmost limit allowed is thirty years, notwithstanding the existence of one or more disabilities during the whole period. (See **STATUTE-BARRED DEBTS.**) In matters connected with real property under this Act of 1874, it will be noticed that not only is the remedy barred, but the right also, whereas in the case of debts the remedy alone is barred, and then only if the Statute of Limitations, 1623, is specially pleaded by the defendant.

An action on an English judgment is also barred after twelve years. A foreign judgment is considered to be on the same footing as a simple contract debt, and consequently proceedings must be taken upon it within six years of the date of the foreign judgment.

By the Trustee Act, 1888, trustees can claim the benefit of the Statutes of Limitation, except in cases of fraud founded upon a fraudulent breach of trust, and also where a trustee has received and converted trust property to his own use.

By the Public Authorities Protection Act, 1893, any action in tort in which a claim for damages is made must be commenced within six months of the date when the right of action arose.

As to other claims in tort, the general rule is that an action may be commenced within six years of the date when the cause of action arose. This rule is subject to two exceptions, namely, an action for slander must be commenced within two years after the publication of the alleged slander, and an action for injuries to the person (including imprisonment) within four years.

It is unnecessary to enter into the various limitations of time imposed by special statutes in the case of certain criminal offences. Such matters are outside the purview of the present work.

LIMITED COMPANY ACCOUNTS.

Before dealing with the actual book-keeping in connection with limited companies it is desirable that something should be said regarding the constitution and formation of joint stock companies. Joint stock companies have existed for several hundred years, but it was not until 1855 that the principle of limited liability was recognised. In 1862 the Joint Stock Companies Act was passed, which gave a great impetus to the formation of companies on this basis. Subsequent to this date a large number of Acts were passed dealing with joint stock companies, and in 1908 the whole were consolidated in the Companies (Consolidation) Act of that year. Since then several amending Acts have been passed, and the statutory law is now to be found in the Companies Acts, 1908-1917. These Acts provide for the formation of companies the liability of whose members is limited to the nominal value of the shares subscribed for by them, to companies limited by guarantee, and to companies the liability of whose members has no limit. In addition to companies formed under these Acts, joint stock companies may be formed by Royal Charter, or by special Act of Parliament, but it is with companies formed under the Companies Acts, 1908-1917, with which this article deals. It may be noted that the Act of 1908 prohibits the association of more than ten persons for the purpose of carrying on the business of banking, or of more than twenty persons for the purpose of carrying on any other business which has for its objects the acquisition of gain, unless such association is registered under the Companies Acts, 1908-1917. The legal minimum required for the formation of a company to be registered under these Acts is two in the case of a private limited company, and seven if the company is to be a public company. A private company is defined by Section 121 of the 1908 Act as amended by Section 1(2) of the 1913 Act as one which, by its Articles restricts the right to transfer its shares, prohibits any invitation to the public to subscribe for any of its shares or debentures, or debenture stock, and limits the number of its members (exclusive of persons who are in the employment of the company and of persons who, having been formerly in the employment of the company were while in such employment and have continued after the determination of such employment to be members of the company) to fifty. In the case of a public company there is no limit to the number of members it may have, except that each member must hold at least one share. The expression "One man company" is sometimes met with, but this has no legal significance. It merely means that the bulk of the shares are held by one man.

FORMATION OF A COMPANY.—From what has been stated above it will be seen that any seven or more persons may be incorporated as a public company (or any two or more persons (not exceeding fifty) may form themselves into a private company). To do this, they must subscribe their names to a Memorandum of Association, and comply with the requirements of the Acts so far as they relate to registration. Such company may be (a) a company limited by shares, in which the liability of each member is limited to the amount unpaid, if any, on the shares for which he subscribes; (b) a company limited by guarantee, *i.e.* one in which the members agree in the event of the company being wound up to contribute to the assets of the company a certain fixed amount; or (c) an unlimited company, *i.e.* a company in which there is no limitation to the liability of the members. In each case the company must have a Memorandum of Association, in which, if the company is limited by shares, the following particulars must be stated—

(a) The name of the company with the word "Limited" as the last word of the name,

(b) The country (part of the United Kingdom) in which the registered office is to be situated,

(c) The object for which the company is to be formed,

(d) A statement that the liability of the members is limited,

(e) The amount of the capital of the company and the division thereof into shares of a fixed amount.

This document must be signed by at least seven persons if the company is to be a public one, and at least two if the proposed company is a private one, and each signatory must enter in the space provided the number of shares which he proposed to take. The signatures must also be attested by a witness. The Memorandum requires stamping as a deed, and must also bear the capital stamp duty in accordance with the table given on page 810.

ARTICLES OF ASSOCIATION.—These are the regulations for the conduct of the internal business of the company, and in the case of a public company limited by shares, special Articles of Association need not be registered with the Memorandum, but if no Articles are registered the company is governed by Table A, which will be found as the first schedule to the Companies Act of 1908. A private company, however, *must* register Articles, owing to the fact that Table A does not contain all the provisions which must be stated in the Articles of a private company. As a matter of practice, special Articles, which either exclude Table A or adopt it with modifications, are registered with the Memorandum of Association in the majority of cases, it being found that Table A does not contain the precise regulations which the company requires. Special Articles are also

necessary in the case of companies limited by guarantee and unlimited companies. These Articles of Association must be signed by the same persons who sign the Memorandum, and the signatures must be witnessed. They must be stamped with a 10s. deed stamp, and also with a 5s. registration stamp.

Another document required before the company can be registered is a Declaration of Compliance with the requirements of the Companies Acts. This has to be signed by a solicitor of the High Court or by a person named in the Articles as a director or secretary of the Company, who declares that the requirements of the Act as to registration of matters precedent and incidental thereto have been complied with. A 5s. registration stamp is required on this declaration. A statement of the nominal capital of the company must also be filed, on which capital duty must be paid at the rate of £1 for every £100 of capital. Other documents which require filing either at the time of registration or immediately afterwards are a list of persons who have consented to be directors of the company; notice of the situation of the registered offices; particulars of directors. It should also be noted that if the directors of a public company are appointed by the Articles they must, before these are registered, sign and file with the Registrar consents in writing to act, and either sign the Memorandum of Association for a number of shares not less than their qualification, or sign and file with the Registrar contracts in writing to take from the company and to pay for their qualification shares. When the above documents have been lodged, and the prescribed fees paid, the Registrar will issue a certificate of incorporation which is conclusive evidence that all the requirements of the Acts in respect of registration and all matters precedent and incidental thereto have been complied with.

COMMENCEMENT OF BUSINESS.—Although a private company may commence business as soon as it is incorporated a public company must first comply with Section 87 of the 1908 Act; namely, the minimum subscription must be allotted subject to the payment of the whole amount in cash; directors must pay in respect of the shares taken or contracted to be taken by them, for which they are liable to pay in cash a proportion equal to the proportion payable by the public on application or allotment; if the company has not issued a prospectus, a statement in lieu of prospectus must have been filed with the Registrar, and also a Statutory Declaration stating that the conditions of Section 87 have been complied with.

When these documents have been filed and are found to be in order the Registrar issues a certificate which entitles the company to commence business.

ISSUE OF SHARE CAPITAL.—After the registration of the company it is usual, if the company is a public company, to appeal to the public to subscribe for its shares. This is usually done by means of a prospectus, which must comply with Sections 80 and 81 of the 1908 Act. A company other than a private company which does not issue a prospectus must file with the Registrar a statement in lieu of prospectus signed by every person named therein as director or proposed director. The form is given in the second schedule of the 1908 Act, and it should be noted that this statement must be filed before any allotment of shares or debentures can be made. If a prospectus is issued it is usual to enclose a form of application to be filled up by the applicant. The applicant is requested to forward to the company's banker with his application a cheque for the amount due on application for the number of shares he applies for. The banker on receiving the applications and the accompanying cheques will enter the amounts in a special pass book, and forward it to the company from time to time together with the corresponding application forms. The forms are numbered and checked with the bank pass book, after which the particulars are entered from the forms on to the application or allotment sheets, a ruling of which is given on page 42. The cash received is entered in a subsidiary cash book in detail, and periodically the total is transferred to the general cash book, from which it is posted to the credit of the application and allotment account. When the application sheets are completed, and the total amount received is checked with the bank pass book, the sheets are placed before the directors and the allotment is proceeded with. It is first necessary to see that the conditions regarding the minimum subscription have been complied with. By minimum subscription is meant the amount fixed by the directors which must be subscribed before the allotment can take place. Section 85 of the 1908 Act provides that a public company which issues a prospectus may not make a first allotment of shares unless within 40 days of the first issue of the prospectus the minimum subscription has been received by the company in cash. The minimum subscription must not include any amount payable otherwise than in cash, but applications of underwriters, if complete and in order and the application money paid, may be taken into account. In this connection it may be noted that cheques until cleared are not cash, and cannot be regarded as amounts paid to and received by the company. If this is in order the directors allot the shares at their discretion, the resolution of allotment is recorded in the Minute Book, particulars of the allotment are entered on the application and allotment sheets, and to those members to whom allotments have

been made letters of allotment are forwarded, while to those to whom no allotment has been made letters of regret are sent. A Journal entry is now made debiting the application and allotment account with the total amount due on application of allotment, and crediting share capital account. As the allotment money is received, it is entered into a subsidiary cash book in detail, and the total is transferred periodically to the general cash book and posted to the credit of the application and allotment account. It will thus be seen that when all the amounts due on application and allotment have been received and posted, the application and allotment account will balance.

In the event of the issue being over-subscribed, some of the applicants may not receive any allotment, while to others will be allotted a smaller number of shares than they applied for. To those applicants who receive no allotment the money paid on application will be returned, in which case an entry will be passed through the cash book and posted in total to the debit of the application and allotment account. In the case of those to whom only a partial allotment is made the amount paid on application is retained and used as a set-off against the amount payable on allotment.

In connection with the allotment, attention may be called to Section 88 of the 1908 Act, which provides that whenever a limited company makes an allotment of shares it must, within one month, file a return showing in the case of shares payable in cash the number and nominal amount of the shares allotted, the names, addresses and descriptions of the allottees, and the amount, if any, due and payable on each share. In the case of shares allotted as fully or partly paid up otherwise than in cash, the return must state the number and nominal amount of such shares, the extent to which they are to be treated as paid up, and the consideration for which they have been allotted. In addition, there must be filed a contract in writing constituting the title of the allottee to the allotment, together with any contract of sale or for services, or for other consideration in respect of which the allotment was made, all such contracts to be duly stamped.

The terms of issue of the shares usually provide that any amount remaining unpaid may be called up by the directors as and when required. When a call is made an appropriate resolution is passed, and notice of the call is sent to each shareholder. A call sheet showing the amount payable by each shareholder is prepared, and a journal entry is made debiting the call account with the total amount due, and crediting the share capital account.

The amounts received in response to the call are dealt with in the same way as in the case of the allotment money; the total is entered periodically in the general cash book and posted

to the credit of the call account. It will thus be seen that the share capital account has been credited with the amounts due on application, allotment, and call, so that, when the full amount of the shares has been called up, the share capital account will have been credited with the full value of the shares issued. The application and allotment account will have been debited with the amount due on application and allotment, and credited with the cash received; consequently, if it shows a debit balance this represents the amount unpaid on allotment. Similarly, if the call account has been debited with the total amount due and credited with the cash received, a debit balance indicates the amount of unpaid calls.

EXAMPLE.—A company offers for subscription 100,000 shares of £1 each, payable 5s. on application, 5s. on allotment, and the balance one month after allotment. The subscription list opened on the 14th July, 19.., and applications were received for 120,000 shares, the company going to allotment on the 18th July, 19..

It will at once be seen that the issue is over-subscribed, and it will be assumed that the over-subscription is returned to the unsuccessful

applicants. The amount thus due on application and allotment on the shares allotted is £50,000, so the first Journal entry will be—

July 18 Application and allotment account *Dr.* £50,000
 To Share Capital Account £50,000
 Being the amount due on application and allotment on 100,000 shares allotted this day in accordance with the resolution of the directors.

When the call is made the following Journal entry will be necessary—

Aug. 18 Call Account *Dr.* £50,000
 To Share Capital Account £50,000
 Being a call of 10s. per share on each of the 100,000 shares made this day in accordance with the terms of the prospectus and resolution of the directors.

The cash received with the applications and in response to the allotment letters and call letters will have been entered in the subsidiary cash book, and the totals transferred periodically to the general cash book. The amounts returned to the applicants will also have been entered in the cash book in total and posted to the debit of application and allotment account. The cash book and ledger account of the issue will therefore appear as under—

<i>Dr.</i> CASH				CONTRA <i>Cr.</i>			
19..				19..			
July 15	To Amount received on application for 120,000 Shares, 5s. each	£	s. d.	July 18	By Deposits refunded	£	s. d.
„ 19	„ Amount received on allotment of 100,000	30,000	0 0			5,000	0 0
Aug. 18	„ Call Account in respect of call of 10s. each on 100,000 shares	25,000	0 0				
		50,000	0 0				

<i>Dr.</i> SHARE CAPITAL ACCOUNT				<i>Cr.</i>			
				19..			
				July 18	By Application and Allotment Account	£	s. d.
				Aug. 18	„ Call Account	50,000	0 0
						50,000	0 0
						100,000	0 0

<i>Dr.</i> APPLICATION AND ALLOTMENT ACCOUNT				<i>Cr.</i>			
19..				19..			
July 18	To Share Capital Account	£	s. d.	July 15	By Cash	£	s. d.
„ „	„ Cash. Deposits refunded	50,000	0 0	„ 19	„ „	30,000	0 0
		5,000	0 0			25,000	0 0
		55,000	0 0			55,000	0 0

<i>Dr.</i> CALL ACCOUNT				<i>Cr.</i>			
19..				19..			
Aug. 18	To Share Capital Account	£	s. d.	Aug. 19	By Cash	£	s. d.
		50,000	0 0			50,000	0 0

A further example is given in which are introduced several additional points. It will be noticed, for instance, that the applications and allotments are dealt with in separate accounts, and that some of the application money is retained not only on account of allotments, but also on account of the calls.

EXAMPLE.—Suppose the formation of a company A Limited with a nominal capital of £150,000 in shares of the denomination of £1, and that the formation expenses are—

(1) Capital Duty	£1,500
(2) Fees and Deed Stamps, Expenses of Memorandum and Articles of Association, printing	325
(3) Legal Charges	50
	<u>£1,875</u>

It adopts an agreement which has been filed at Somersset House for the purchase of a property for the sum of £35,000, payable as to £10,000 in cash and £25,000 by the allotment of fully paid shares, and it is resolved to offer to the public for subscription 60,000 shares of £1 each at a premium of 2s. per share. Due compliance has been made with the requirements of the Registrar of Joint Stock Companies, including the filing of the prospectus, and the necessary arrangements have been made with the company's bankers for the reception of subscriptions. The issue is underwritten for a commission of $2\frac{1}{2}$ per cent. and an over-riding commission of 1 per cent. A brokerage of 3d. per share is payable. The subscription is payable as to

4s. per share on application (including the premium)
6s. " " " allotment
6s. " " " first call
6s. " " " second call

and it is assumed that the calls are duly made.

Let us suppose that the total number of shares applied for is 62,000, that the total amount received on application is £12,400, and that the following shows the result of the allotment—

Total amount received on application	£12,400
of which there is returned to applicants	200
leaving	12,200
of which there is applied to payments due on allotment	80
leaving	12,120
of which there is applied to payments due on first call account	60
leaving	12,060
of which there is applied to payments due on final call account	60
leaving	<u>£12,000</u>

which represents 60,000 shares at 4s. per share.

There is thus to receive on—

<i>Allotment</i> 60,000 shares at 6s.	18,000	£
Less amount already received	80	
	<u>17,920</u>	
<i>First Call</i> 60,000 shares at 6s.	18,000	
Less amount already received	60	
	<u>17,940</u>	
<i>Final Call</i> 60,000 shares at 6s.	18,000	
Less amount already received	60	
	<u>17,940</u>	
Total	<u>£53,800</u>	

The first entry in the Share Journal, after allotment of the 60,000 shares, would be—

Application Account	£12,000	£
To share Capital Account	6,000	
" " Premiums Account	6,000	
For amount payable on application on 60,000 shares of £1 each at 4s. per share inclusive of premium.		

Entries similar to the foregoing would be required for the Allotment Account and First and Second Call Accounts.

The ledger accounts, *pro forma* of the issue, assuming that all the shareholders have discharged their obligations, are—

SHARE CAPITAL ACCOUNT

By Application A/c	£6,000
" Allotment A/c	18,000
" First Call A/c	18,000
" Final Call A/c	18,000
	<u>£60,000</u>

APPLICATION ACCOUNT

To Cash (amount ret'd)	£200	By Cash	£12,400
" Allotment A/c	80		
" First Call A/c	60		
" Final Call A/c	60		
" Share Premium A/c	6,000		
" Share Capital A/c	6,000		
60,000 share as 2s.			
	<u>£12,400</u>		<u>£12,400</u>

ALLOTMENT ACCOUNT

To Share Capital A/c	£18,000	By Application A/c	£80
60,000 shares at 6s.		" Cash	17,920
	<u>£18,000</u>		<u>£18,000</u>

FIRST CALL ACCOUNT

To Share Capital A/c	£18,000	By Application A/c	£60
60,000 shares at 6s		" Cash	17,940
	<u>£18,000</u>		<u>£18,000</u>

FINAL CALL ACCOUNT

To Share Capital A/c	£18,000	By Application A/c	£60
60,000 share at 6s.		" Cash	17,940
	<u>£18,000</u>		<u>£18,000</u>

SHARE PREMIUM ACCOUNT

By Application A/c	£6,000
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The company agreed in the prospectus to pay a brokerage of 3d. per share on all allotments due to applications bearing the stamps of brokers and others. It is therefore necessary to examine all the applications carefully, and to prepare a statement showing the amount of the company's obligation under this head, *e.g.*—

	No. shares applied for.	No. shares allotted.	£	s.	d.	£	s.	d.
A. B. Booker applied for.								
J. Jones	200	150 at 3d.	1	17	6			
R. Thomas	100	100 at 3d.	1	5	0			
						3	2	6

W. A. Rutter
M. Blue 300 280 at 3d. 3 10 0
etc., etc., the amount totalling £560 as per Cash Book entry.
The underwriting commission is $3\frac{1}{2}\%$ on £60,000 = £2,100.

When the shares are allotted in satisfaction of the purchase of the property the Journal entry will be worded somewhat as follows—

Vendors	£25,000
To Share Capital Account	£25,000
For allotment as fully paid of 25,000 shares numbered inclusive in satisfaction of purchase of property	
as per purchase agreement dated	
and as per Board Minute dated	

We may now assume at this stage the entries in the ordinary Cash Book (*pro forma*) (see below.)

On the basis of the transactions which we have passed in review the trial balance of the ledger will be found as under—

	Dr.	Cr.
Share Capital Account		£85,000
Share Premium Account		6,000
Property Account	£35,000	
Bank	51,465	
Share Capital Issue Expenses	2,660	
Preliminary Expenses	1,875	
	£91,000	£91,000

Commonly the share capital issue expenses are written off the premium, and if it be resolved to write off also the preliminary expenses we should have the balance of the premium account appearing in the Balance Sheet at £1,465, viz.—

Share Premium Account—	£	£	£
Premium of 2s. per share on the issue of 60,000 shares of £1 each		£6,000	
Less amounts written off—			
Preliminary Expenses	1,875		
Share Issue Expenses, including commission and brokerage.	2,660		
		4,535	
			1,465

To Share Capital—	£
„ Application Account	12,400
„ Allotment Account	17,920
„ First Call Account	17,940
„ Second Call Account	17,940
	£66,200
To Balance	£51,465

As soon as the allotment money has been paid, it may be decided (if the calls are not payable until a considerable time after allotment) to issue certificates to the various shareholders stating the amount paid in respect of the shares, with a form on the back of each certificate for the subsequent payment of calls to be endorsed thereon as and when received.

In the above example it will be noticed that the shares are issued at a premium. In such cases the premium is carried to a separate account called Premium on Shares Account. The premium represents profit to the company, but as it is capital profit it is not usual to regard it as being available for dividends, though there does not appear to be any legal objection to its being used for this purpose unless the Articles prevent it. In some businesses the premium on shares is maintained as a reserve, while in others it is used, as shown in the example above, for writing down fictitious assets.

SHARE LEDGER.—In connection with the application and allotment of shares, reference may be made to a subsidiary book which is brought into use at this time, namely, the Share Ledger, which, for convenience, is usually combined with the Register of Members. The Share Ledger contains the share account of each member, although it is not regarded as one of the financial books of the company, but is more in the nature of a statistical book. The ruling of a Share Ledger will be found in the article on MEMBERS, REGISTER OF, where it is combined with that register. The essential features of the Share Ledger are that it contains on the debit side a record of the amounts payable on the shares held by each member, and on the credit side particulars of the amounts actually paid by the member. Immediately an allotment of shares or a call is made, each member's account is debited in the Share Ledger with the amount due from him on application and allotment, or on the call. The particulars of these debits are obtained from the application and allotment sheets, and the call sheets respectively. As the amounts are received they are, as has already been stated, entered in a subsidiary cash book, and thence transferred to the credit of the individual shareholders' accounts in the Share Ledger. A reference to

By Application Account (amount returned to applicants)	£	£
„ Preliminary Expenses		200
„ Purchase of Property		1,875
„ Share Capital Issue Expenses—		10,000
Commission	2,100	
Brokerage	560	
		2,660
„ Balance		51,465
		£66,200

the account of any shareholder at once shows whether or not the amounts due from him have been paid.

MONEY PAID IN ADVANCE OF CALLS.—If so authorised by its Articles a company may accept from any member the whole or a part of the amount remaining unpaid on any shares held by him, although no part of the amount has been called up. Most companies make this provision in their Articles, and also usually provide for payment of interest by the company on the amounts thus paid in advance. Where such an arrangement is made the interest is payable even though no profit is made. It may also be noted that, in the event of the company going into liquidation, money so advanced must be refunded before any repayment of the shares is made in respect of called up capital, but no money may be returned while the company is a going concern. When money is paid in advance of calls it should be entered in a separate account in the Ledger, as, until the call is made, it forms no part of the capital of the company. When subsequently a call is made the amount standing to the credit of the calls in advance account is transferred to the credit of the share capital account. The interest paid on money received in advance of calls is debited to interest account and credited to the shareholders.

INTEREST ON CALLS IN ARREAR.—The Articles of Association of most companies provide for the charging of interest on calls not paid within the specified time. Where such a clause becomes operative the shareholder is debited with the amount of the interest, and interest receivable account is credited.

PURCHASE OF A BUSINESS.—When a company is formed for the purpose of taking over an existing business, an agreement is usually entered into, one of the clauses of which deals with the amount to be paid for the business, and the manner in which payment is to be made. It frequently happens that the newly formed company takes over the assets and liabilities of the business at the valuation shown in the last balance sheet, or at an agreed valuation. The purchase money is usually paid partly in shares in the new company and partly in cash. As regards the books of the new company it is necessary to bring into them the assets acquired and the liabilities undertaken, and this is done through the medium of Journal entries, the effect of which is that the assets acquired are debited to the various accounts and credited to the vendor's account. The vendor is then debited with the liabilities taken over by the company, and these are credited to their respective accounts in the books of the company. The vendor's account will then show a credit balance which represents the purchase price, and this is discharged by allotting to him the agreed number of shares, and by paying to

him the cash as arranged in the agreement. If it happens that the purchase price, plus the liabilities which the company has agreed to take over, exceeds the value of the assets acquired, the balance is regarded as the amount paid for the goodwill of the business, and is accordingly debited to a goodwill account. In illustration of the above procedure the following example is submitted—

A joint stock company which has a registered capital of £180,000, consisting of 105,000 ordinary shares of £1 each, and 75,000 10 per cent. preference shares of £1 each, purchases as a going concern for £100,000 a business on the basis of the following balance sheet—

<i>Liabilities.</i>		<i>Assets.</i>	
	£		£
Bills Payable	7,500	Cash	3,000
Sundry Creditors	12,500	Bills Receivable	1,500
Capital	70,000	Book Debts	26,500
		Freehold Premises	30,000
		Plant and Machinery	15,000
		Stock	12,000
		Furniture and Fittings	2,000
	£90,000		£90,000

The price to be paid for the business was £50,000 in fully paid ordinary shares, £25,000 in fully paid preference shares, and the balance in cash. Show the Journal entries necessary to incorporate these transactions in the books of the company.

In the first place it should be noticed that the assets, less the liabilities taken over, amount to £70,000, and that the purchase price paid for the business is £100,000. The amount which is being paid for the Goodwill is thus £30,000, which must be brought into the books. The Journal entries would appear as follows—

	£	£
Cash	3,000	
Bills Receivable	1,500	
Debtors	26,500	
Freehold Premises	30,000	
Plant and Machinery	15,000	
Stock	12,000	
Furniture and Fittings	2,000	
Goodwill	30,000	
To Vendor		120,000
For Sundry Assets acquired under agreement dated		
Vendor	20,000	
To Bills Payable	7,500	
Sundry Creditors	12,500	
For Sundry Liabilities taken over under agreement dated		

	£	£
Vendor	100,000	
To Ordinary Share Capital Account		50,000
„ Preference „		25,000
„ Cash		25,000
For payment of purchases price of business acquired under agreement dated		

When the above items are posted it will be found that the vendor's account balances, and that the company has in its books a record of the values of the assets acquired and of the liabilities taken over.

FORFEITURE OF SHARES.—When a call has been made on shares and some of the shareholders

do not pay, it is the duty of the directors to use all legal means to enforce payment. There are, however, occasions when the shareholder is not in a position to meet his liability, in which case the directors may declare the shares forfeited. It should be carefully noted that for a forfeiture to be valid there must be express power in the Articles, the power must be used only in a proper case, and must be carried out strictly in accordance with the Articles, as the slightest departure from the procedure there laid down might invalidate the forfeiture. When the necessary resolution of forfeiture has been duly passed it becomes necessary to give effect to it in the financial books of the company. The method usually adopted is to debit the Share Capital Account with the amount which has been called up on the forfeited shares, to credit the various call accounts on which the default has been made, and to credit Forfeited Shares Account with the amount which the shareholder has already paid. For example: if the directors resolve that 160 shares on which 15s. each per share has been called up shall be forfeited, owing to the non-payment of the first and second calls of 5s. each, this would be journalised as follows—

Share Capital Account	£120
To First Call Account	£40
" Second " " "	40
" Forfeited Shares Account	40

The effect of the posting of this entry is—

(1) The Share Capital Account, which had previously been credited with the amount called up, is reduced by the called-up value of the forfeited shares.

(2) The first and second call accounts, which were debited with the amount of the call when made, are credited with the amount due but not paid.

(3) The Forfeited Shares Account receives credit for the amount paid by the share but now forfeited. This amount represents a gain of the company, but being a capital profit is usually transferred to a reserve and used for the writing down of capital expenditure or losses.

This, however, should not be done if there is any intention of re-issuing the forfeited shares.

RE-ISSUE OF FORFEITED SHARES.—Forfeited shares may be re-issued if the Articles of a company so provide and the re-issue may be at a premium, at par, or even at a discount, provided

the discount does not exceed the amount already paid on the shares by the former owner. When such re-issue takes place the transaction is journalised as indicated below. If the re-issue is at par, debit shareholder, credit share capital account. The effect of this is to restore the capital account to its original amount and the shareholder becomes a debtor for the amount charged for the shares. If issued at a discount, the capital account is credited with the called-up value of the shares, the buyer is debited with the amount he agrees to pay, and the difference is debited to the forfeited shares account. In other words, the loss on the re-issue is charged against the amount which was previously credited to forfeited shares account. As an illustration, suppose the shares referred to above were re-issued to A B, credited with 15s. per share paid up, for £100. The Journal entry would be—

A B	Dr.	£100
Forfeited Shares Account		20
To Share Capital Account		£120

Re-issue of 150 shares at £1 each credited with 15s. per share paid for £100 as per resolution dated

DEBENTURES: ISSUE OF.—Debentures are issued on the same lines as indicated in the case of shares, but whereas shares may not be issued at a discount, this is frequently done with debentures, which may, therefore, be issued at a premium, at par, or at a discount. When issued at a discount the practice is to debit the amount of the discount together with the expenses of issue to a separate account entitled Discount on Debentures Account. As this represents a loss to the company it should be written off over a period of years or during the period of the debentures if the debentures are redeemable. Until the discount is written off the balance of the account appears in the Balance Sheet on the assets side. This is in accordance with Section 90 of the 1908 Act, which provides: "Where a company has paid any sums by way of commission in respect of any shares or debentures, or allowed any sums by way of discount in respect of any debentures, the total amount so paid or allowed or so much thereof as has not been written off shall be stated in every balance sheet of the company until the whole amount thereof has been written off." The following illustrates the entries necessary for an issue of debentures at a discount—

CASH

CONTRA

		£	s.	d.					
19..									
Jan. 2	To Debenture Application and Allotment Account								
	Cash on Application	4,000	0	0					
" 6	" Debenture Application and Allotment Account								
	Cash on Allotment	16,000	0	0					
Feb. 6	" Debenture Call Account	16,000	0	0					

Dr				DEBENTURES ACCOUNT				Cr.			
				19..				£	s.	d.	
				Jan. 5	By Debentures Application and Allotment Account . . .			20,000	0	0	
				" "	" Discount on Debentures Account . . .			4,000	0	0	
				Feb. 5	" Debenture Call Account . .			16,000	0	0	
								40,000	0	0	

Dr.				DEBENTURES APPLICATION AND ALLOTMENT ACCOUNT				Cr.			
19..		£	s. d.	19..		£	s. d.				
Jan. 5	To Sundries	20,000	0 0	Jan. 2	By Cash	4,000	0 0				
				" 6	" "	16,000	0 0				
		20,000	0 0			20,000	0 0				

Dr.				DEBENTURES CALL ACCOUNT				Cr.			
19..		£	s. d.	19..		£	s. d.				
Feb. 5	To Debentures Account . . .	16,000	0 0	Feb. 6	By Cash	16,000	0 0				

Dr.				DISCOUNT ON DEBENTURES ACCOUNT				Cr.			
19..		£	s. d.								
Jan. 5	To Debentures Account . . .	4,000	0 0								

EXAMPLE.—A company offers for subscription 400 debentures of £100 each, at a discount of 10 per cent., payable £10 on application, £40 on allotment, and £40 one month after allotment. The issue is fully subscribed.

JOURNAL ENTRIES

19..		£	£	
Jan. 5	Debenture Application and Allotment Account . Dr.	20,000		
" "	Discount on Debentures Account . . . Dr.	4,000		
	To Debenture Account . . .		24,000	
	<i>Being amount due on Application and Allotment of 400 Debentures of £100 each, issued at a discount of 10% allotted this day as per minute of the Directors, No.....</i>			
Feb. 5	Debenture Call Account Dr. .	16,000		
" "	To Debenture Account . . .		16,000	
	<i>Being amount due in respect of Call of £40 on each of 200 Debentures of £100 each, made this day as per Minute of the Directors, No.....</i>			

In order to show how the discount may be dealt with let it be supposed that a limited company issued £4,000 debentures at a discount of 5 per cent. repayable at the end of five years. In this case the discount, which amounts to £200, can be written off at the rate of £80 each year, the entry being a debit to profit and loss account, and a credit to discount on debentures account. The

outstanding balance of the discount on debentures account would be brought down each year as an asset as required by Section 90 referred to above. Take another case: If the above debentures were redeemable by annual drawings of £800 the discount could be treated on the following lines. The debentures outstanding for the first year would be £4,000, for the second year £3,200, for the third £2,400, for the fourth £1,600, for the fifth year £800, the total being £12,000. The company has thus had the use of £12,000 during five years, but in the first year it had the use of £4,000, so that in this year the profit and loss account ought to be charged with $\frac{4,000}{5}$ or one-third of the discount, namely, £66 13s. 4d. Similarly, in the second year the amount of which the company had the benefit was £3,200, consequently $\frac{3,200}{5}$ of the discount is the amount chargeable, and so on for subsequent years.

INTEREST ON DEBENTURES.—This is nearly always paid less tax. When the interest becomes due debenture interest account is debited with the gross amount, the credit being to the debenture holders account. At the same time the debenture holders account is debited with the tax deducted, and this is carried to the credit of the income tax adjustment account. On the dispatch of the interest warrants an entry will be made in the cash book debiting debenture holders account and crediting bank.

REDEMPTION OF DEBENTURES. (See article on DEBENTURES.)

DIVIDENDS.—The manner in which the profits of a company are to be distributed is usually contained in the Articles of Association, although sometimes the Memorandum of Association deals with this matter. The dividend to be paid is proposed by the directors at a general meeting of the company, and if sanctioned by the necessary majority the dividend warrants can be dispatched. It is usual for the company to pass a resolution authorising the closing of the Share Registers and Transfer Registers for, say, 14 days previous to the date of the general meeting in order that the preparations for the payment of the dividend may be undertaken. During this period the dividend lists are prepared and compared with the Register of Members, the warrants are made out and checked, the envelopes addressed, so that all is ready for dispatch when the resolution authorising payment of the dividend is passed. The following is a common form of ruling for the Dividend Sheets—

.....Company, Limited
.....dividend atper share or per cent. payable

No. of Warrant	Payee	Share Ledger Folio	No. of Shares	Dividend	Income Tax account	Amount of Warrant	Remarks

It may not be out of place to remind readers that the dividends must not be paid out of capital except in the special circumstances mentioned in Section 91 of the 1908 Act which are set out below, and that if dividends are wilfully paid out of capital, directors may be liable to make good to the company any amount so paid. Moreover, shareholders who with knowledge of the facts have received a dividend out of capital cannot bring an action against the directors for restitution, and if the directors have been compelled to make restitution of the money illegally paid such shareholders may be called upon to indemnify the directors. Section 91 provides as follows—

“Where any shares of a company are issued for the purpose of raising money to defray the expenses of the construction of any works or buildings, or the provision of any plant which cannot be made profitable for a lengthened period, the company may pay interest on so much of that share capital as is for the time being paid up for the period and subject to the conditions and restrictions in this section mentioned, and may charge the same to capital as part of the cost of construction of the work or building, or the provision of plant :

“Provided that—

“(1) No such payment shall be made unless the

same is authorised by the articles or by special resolution :

“(2) No such payment whether authorised by the articles or by special resolution, shall be made without the previous sanction of the Board of Trade :

“(3) Before sanctioning any such payment the Board of Trade may, at the expense of the company, appoint a person to inquire and report to them as to the circumstances of the case, and may, before making the appointment, require the company to give security for the payment of the costs of the inquiry :

“(4) The payment shall be made only for such period as may be determined by the Board of Trade ; and such period shall in no case extend beyond the close of the half-year next after the half-year during which the works or buildings have been actually completed or the plant provided :

“(5) The rate of interest shall in no case exceed 4 per cent. per annum, or such lower rate as may for the time being be prescribed by Order in Council :

“(6) The payment of the interest shall not operate as a reduction of the amount paid up on the shares in respect of which it is paid :

“(7) The accounts of the company shall show the share capital on which, and the rate at which, interest has been paid out of capital during the period to which the accounts relate.”

On the declaration of a dividend, the entries in the books of account would be : first a debit to dividend account of the gross amount, and a credit to sundry shares (dividend account); the amount of tax, if tax is deducted, is then debited to sundry shares (dividend account) and credited to income tax adjustment account. A cheque for the whole amount payable is usually drawn, and paid in to the credit of a separate bank account, against which the dividend warrants are drawn. Should there be any dividends unclaimed at the date of the balance sheet a journal entry would be made debiting sundry shares (dividend account) and crediting bank dividend account. This entry could be written back on the first day of the new period, or a journal entry can be made when the outstanding dividend amounts were all cleared, or an adjustment could be made at the next balancing period whichever happens first. It may be of interest to note that if the dividends on cumulative preference shares fall into arrears it is not necessary to show such arrears in the financial books of the company, but the usual practice is to make a note on the balance sheet to the effect that the dividend on the cumulative preference shares is so many years in arrears.

ALTERATION IN CAPITAL.—The alteration of the capital clause in the Memorandum of Association of a company is sanctioned by various

sections of the 1908 Act. For instance, by Section 41 a Company may, if so authorised by its Articles :

- (a) Increase its capital,
- (b) Consolidate its capital into shares of larger amounts,
- (c) Convert paid up shares into stock,
- (d) Sub-divide its shares into shares of a smaller amount,
- (e) Cancel shares which have not been taken up.

The resolution to be passed authorising the alteration of the capital depends on the Articles, except that in the case of sub-division the Act itself stipulates that a special resolution is necessary. When an alteration is made every Memorandum of Association issued after the date of the alteration must be in accordance therewith.

INCREASE.—An increase of capital may be either of the subscribed capital or of the authorised capital. In the former case it merely means an issue of further shares in the capital already authorised, and this requires the consent of the directors only. If, however, the increase is to be of the authorised capital then Section 41 must be complied with. This section states *inter alia* that the company may if so authorised by its Articles increase its share capital by the issue of new shares of such amount as it thinks expedient. If the Articles do not contain the necessary authority, these will have to be altered. When the resolution authorising the increase has been passed, notice of the increase must be given to the Registrar within 15 days. It must be on the prescribed form, impressed with a fee stamp and also a registration stamp of 5s. A statement of the increase in capital is also required, the stamp on this document being at the rate of £1 for every £100 of capital, plus a registration stamp of 5s. In the issue of the new share capital, regard must be had to any articles which relate to share capital, *e.g.* they may provide that the new shares shall first be offered to existing shareholders.

When the new capital is issued the applications, allotments, etc., are dealt with in the same manner as the original capital.

BALANCE SHEET OF EXISTING POSITION OF COMPANY

6% Cumulative Preference Stock	£ 400,000	Investments	£5,400,000	£
7% Non-cumulative Preference Stock	Ranking equally in a distribution of Assets. 900,000	Less Reserve	700,000	
6% Preferred Ordinary Non-Cumulative Stock				4,700,000
Deferred Ordinary Stock	1,100,000	Other Assets		45,000
	600,000	Debtors and Debit Balances		121,000
		Cash		40,000
Debenture Stock (4 and 5 %)	3,000,000			
Creditors and Credit Balances	1,800,000			
Debenture interest accrued	16,000			
Revenue Account	40,000			
	50,000			
	£4,906,000			£4,906,000

REORGANISATION AND REDUCTION OF CAPITAL.—From varying causes and circumstances which it is unnecessary to discuss here, reorganisation and its not unusual concomitant of the reduction of the capital of companies, become now and then imperative, with the object of establishing some justifiable relation between the values of assets and capital, and of endeavouring to afford an equitable return on the re-arranged capital, which is more or less impossible on the capital as it exists, thus improving, if possible, its market value. When several classes of share or stockholders with different capital and other rights are concerned, the work of arriving at a solution which will give reasonable satisfaction to the opposing interests involved, is frequently strewn with difficulties.

No scheme of reduction of capital can be carried through which does not receive the approval of each class of stock-holder.

All proposals for the reduction of capital, particularly in cases where various classes of shares or stock are concerned, should be accompanied by such a scheme of reorganisation or re-arrangement as will, as far as can be seen, enable satisfactory dividends to be paid on the reduced capital. Invariably there must be compensating concessions or sacrifices on the part of each class interest.

The benefits to be derived from any scheme of reduction of capital which can be characterised as being successful, can only be realised if the company is enabled by its profits to return satisfactory and improving dividends on its reduced capital, a fundamental condition which should be always borne in mind.

The creditors being satisfied that their interests are not imperilled, the necessary resolutions having been passed, the sanction of the Court obtained, and the provisions of the Companies Acts having been complied with, the existing capital position may be terminated and the scheme authorised brought into being in lieu thereof.

Take, for example, the following condensed outline—

There are non-interest-bearing income certificates, redeemable out of profits only, viz., £300,000, the certificates (representing arrears of preference dividends unpaid) having been issued upon a former re-arrangement of capital.

For some years the average yearly amount available for dividend purposes and carry forward, after providing substantial reserves, has been some £76,000, which is improving, and which the directors consider can be at least maintained.

The capital and income certificate requirements are—

6% cumulative Preference Stock	£ 24,000	
7% non-cumulative do.	63,000	
Any surplus profits to the extent of £132,000 may be applied as to—		
One-half Preferred Ordinary Stock	66,000	
One-half Income Certificates	66,000	(Until the extinction of income certificates amounts to £300,000)
Omitting any return on the deferred Ordinary Stock.		
	<u>£219,000</u>	

A scheme of re-organisation, necessitating the consolidation and reduction of capital is proposed

and sanctioned, the loss to be written off the investments.

The table below sets forth the main features of the sanctioned scheme as it affects the accounts.

The new authorised capital to be, say—

£1,000,000 6% cumulative Preference Stock, possessing rights of priority in a distribution of capital, but not to any further share in profits or capital.	
£2,000,000 Ordinary Stock entitled to all surplus profits and capital.	
	<u>£3,000,000</u>

The Balance Sheet (*pro formâ*) with the altered capital, after having made the necessary book entries, may be stated as on the next page.

Proposed schemes of capital re-organisation and reduction are usually attended by so many diverse factors and circumstances, and assume so many varied phases, that it is impossible to enter further into the subject owing to space limitations.

RECONSTRUCTION AND AMALGAMATION.—

It is not necessary to enter into any lengthy dissertation upon the reconstruction of public companies. When, for financial and other reasons,

Existing Capital and Income Certificates.	£	£	Changes sanctioned.	Amount of Capital and Income Certificates lost or to be surrendered by holders.
6% Cumulative Preference Stock	400,000			£
7% Non-Cum. Preference Stock	900,000	300,000 600,000 900,000	to be converted into 6% Cum. Pref. Stock to be converted into new Ordinary Stock	
6% Pref. Ordinary Non-cum.	1,100,000	550,000 550,000 1,100,000	to be written off to be converted into new Ordinary Stock	550,000
Deferred Ordinary	600,000	400,000 200,000 600,000	to be written off to be converted into new Ordinary Stock	400,000
Total Capital	3,000,000	100,000 200,000 300,000	to be written off to be converted into new Ordinary Stock	100,000
Add Income Certificates	300,000			
Total Capital and Income Certificates	3,300,000		Total	<u>1,050,000</u>

BALANCE SHEET (PRO FORMA)

6% Cumulative Preference Stock	£ 700,000	Investments	£ 4,700,000
Ordinary Stock	1,550,000	Less amount written off under scheme of re-organisation and reduction of capital	750,000
	<u>2,250,000</u>		<u>3,950,000</u>
Debenture Stock (4 and 5 %)	1,800,000	Other Assets	45,000
Creditors and Credit Balances	16,000	Debtors and Debit balances	121,000
Debenture Interest accrued	40,000	Cash	40,000
Revenue Account	50,000		<u>£4,156,000</u>
	<u>£4,156,000</u>		

a company determines to transfer its property to another company to be formed for that and probably other purposes, which means the winding up of the old company and the formation of a new company to acquire its property, the process bears the appellation of reconstruction. If, instead of transferring the assets and liabilities to a new company to be formed for that or other purposes, it is proposed to transfer them to an existing company, the process or act is usually termed amalgamation or absorption; but none of these terms—reconstruction, amalgamation, or absorption—has any precise legal significance beyond that stated. They are merely terms adopted by usage. The term reconstruction does not appear in any statute; that of amalgamation is to be found in the Assurance Companies Act, 1909, and in the Railway Clauses Act, 1863. In the former case its use means a transfer of the business of two or more life assurance companies to a third; and in the latter it means the transfer by two or more companies to a new company, or by one or more companies to an existing company.

It is important to note that the reconstruction agreement commonly provides *inter alia* that the consideration of the transfer of the undertaking shall be—

- (1) The formation of a new company.
- (2) The issue of partly paid-up shares.
- (3) The discharge of the liabilities of the old company and all costs, charges and expenses of, and incidental to, the winding-up of the old company, including the remuneration of the liquidator.
- (4) The discharge of all costs and expenses of, and incidental to, the preparation and carrying out of the agreement, and the formation and registration, or preliminary expenses, of the new company, including registration fees and transfers of the assets of the old company to the new.

Let us assume the following data and construct a practical case with a minimum of legal phraseology.

The X Y Z Co., Ltd., passes the usual resolutions to enter into voluntary liquidation for reconstruction, the issued and paid-up capital

being 500,000 shares of £1 each. The new Co., A B, Ltd., is formed with a nominal capital of 1,000,000 shares of £1 each, and the scheme of reconstruction provides for the issue of 749,993, each creditor with 15s. paid, 1s. per share to be paid on application and 2s. per share on allotment, each shareholder in the old company being entitled for every three shares held in that company, to an allotment of four shares, partly paid as indicated, in the new company, which is part consideration for the transfer of the undertaking of X Y Z, Ltd., to A B, Ltd.

The shareholders may dissent in due form as provided by the provisions of the Companies (Consolidation) Act, 1908.

The shareholders may renounce their right to an allotment of shares in the new company in favour of one or more parties.

Dissentient interests to be satisfied is a matter for negotiation, and possibly arbitration, and as regards the proportion of the shares in the new company, which, but for their dissent, would have been claimable by those members of the old company who effectually dissent from the special resolutions, the liquidator shall use his best endeavours to sell for what they will fetch the rights to apply for and receive an allotment of the shares credited as indicated. The net proceeds, after deducting all expenses of, and incidental to, the sale, are to be applied in or towards payment of the amounts which shall become payable to dissentients, and in so far as the sum shall be deficient, the new company shall make up the deficiency.

As regards that proportion of the shares in the new company which members of the old company, other than dissentient members, shall be entitled to claim, but shall not within the period of fourteen days claim, the liquidator is to use his best endeavours to sell the right to apply for and receive an allotment of such shares for what they will fetch. The net proceeds of sale, after paying all expenses of, and incidental to, the sale, have to be distributed rateably among the members who, if they had claimed, would have been entitled to such shares in accordance with their rights and interests, and the new company will, on the

request of the liquidator, allot the shares sold to the purchasers credited as indicated, but such request, to be effective, must be made within three calendar months from date.

No shares credited with 15s. paid will be issued after the expiration of three months.

Every person, not being a shareholder in the old company, applying for "excess" or "surplus" shares (15s. paid) in the new company must tender a certain sum, or an amount per share, in addition to paying the liability of 5s. per share in accordance with the terms of issue. Similarly in regard to those who are shareholders, they must tender a fixed sum, or a price per share, for any shares they apply for in excess of those to which they are entitled as a matter of right in the reconstruction scheme.

The seven signatories' shares are paid for in full in cash.

We can now proceed to construct our practical example. The statement at foot of page sets forth the results of the issue.

The following persons, not being shareholders in the old company, applied for and were allotted the following shares—

Name.	No. of Shares.	Amount of Tender.
R	3,000	£150
S	2,000	100
T	1,000	50
	<u>6,000</u>	<u>£300</u>

The following persons, being shareholders in

the old company, applied for and were allotted the following shares in excess of their rights—

Name.	No. of Shares.	Amount of Tender.
A	5,000	£20
C	1,000	5
	<u>6,000</u>	<u>£25</u>

The result, therefore, is as under—

	No. of Shares.	
A	80,000	
B	1,000	
P	500	
C	4,000	
Q	7,500	7 Signatories' 739,000
K	140,000	Shares paid in full.
L	300,000	
M	200,000	Total £739,007
R	3,000	
S	2,000	
T	1,000	
	<u>739,000</u>	

Let us suppose the balance sheet (*pro formâ*) of the old company at the commencement of the reconstruction to be as under—

Share Capital	£ 500,000	Property	£ 500,000
Sundry Creditors	3,000	Sundry Debtors	4,000
Reserve	2,000	Cash	600
Profit and Loss	500		
	<u>£505,500</u>		<u>£505,500</u>

and assume the following—

The liquidator realises the debtors for £2,700

SHAREHOLDING INTERESTS IN THE OLD COMPANY.		No. of Shares in new Company to which entitled as of right.	DISSENTIENTS.		SHAREHOLDERS IN THE OLD COMPANY WHO			Who neither dissented, assumed their rights, nor transferred them.	
Name.	Holding.		No. of Shares.	Cost of purchasing their Interests.	Assumed their Rights.	and applied for and were allotted Shares in excess of Rights.	and who wholly or partially transferred their rights in favour of		
							Name.	No.	No.
A	50,000	75,000	—	£ —	75,000	5,000	—	—	—
B	1,000	1,500	—	—	1,000	—	P	500	—
C	2,000	3,000	—	—	3,000	1,000	—	—	—
D	5,000	7,500	—	—	—	—	Q	7,500	—
E	500	750	—	—	—	—	—	—	750
F	100	150	—	—	—	—	—	—	150
G	50	75	50	2	—	—	—	—	—
H	50	75	—	—	—	—	—	—	75
I	400	600	400	10	—	—	—	—	—
J	900	1,350	—	—	—	—	—	—	1,350
K	100,000	150,000	—	—	140,000	—	—	—	—
L	200,000	300,000	—	—	300,000	—	—	—	—
M	139,000	208,500	—	—	200,000	—	—	—	—
N	500	750	—	—	—	—	—	—	750
O	500	750	—	—	—	—	—	—	750
TOTAL	500,000	750,000	450	12	719,000	6,000	—	8,000	3,825

and pays the registration and other fees of the new company, say £500, other preliminary expenses on behalf of the new company amounting to £175; he also discharges, and the new company remits to the liquidator, a cheque for £1,075, which with the amount in hand discharges all liabilities, including the liquidator's fee of £100, the liquidator's Cash Account being as under—

LIQUIDATOR'S CASH ACCOUNT			
		£	£
Sundry Debtors	2,700	Registration fees for A/c of new Company	500
New Company	1,075	Other Preliminary Expenses of New Company	175
		Liquidation Fee	100
		Sundry Creditors	3,000
	<u>£3,775</u>		<u>£3,775</u>
NOTE.—£1,075 =			
		Registration Fees	£500
		Other Expenses	175
		Liquidation Fee	100
			<u>775</u>
		On A/c of Creditors	300
			<u>£1,075</u>

The tender money received by the new company is paid over to the liquidator for distribution among the shareholders of the old company. Assuming the new company to have paid £1,000 by way of underwriting commission and the due receipt of the application and allotment money, and call money of 2s. per share, we may frame our commencing accounts as under—

LIQUIDATOR OF X Y Z, LTD.			
Share Capital—		£	£
729,000 shares, 15s.	554,250	Purchase a/c	554,250
APPLICATION AND ALLOTMENT ACCOUNT			
Share Capital—		£	£
7 Sig. Shares, £1	7	Cash	7
739,000 Shares, 3s.	110,850	Do.	110,850
	<u>£110,857</u>		<u>£110,857</u>
CALL ACCOUNT			
Share Capital—		£	£
739,000 Shares, 2s.	73,900	Cash	73,900
PURCHASE OF X Y Z UNDERTAKING			
Liquidator		£	
Cash	554,250		
	<u>1,075</u>		
	<u>£555,325</u>		
UNDERWRITING COMMISSION			
Cash		£	
	<u>1,000</u>		
LIQUIDATOR OF OLD COMPANY			
Cash		£	£
	<u>325</u>	Cash	<u>325</u>

SHARE CAPITAL ACCOUNT			
			£
Application and Allotment Account—			
7 Shares at £1	7		
739,000 Shares at 3s.	110,850		
Call Account—			
739,000 Shares at 2s.	73,900		
Liquidator—			
739,000 Shares at 15s.	554,250		
			<u>£739,007</u>
CASH			
		£	£
Sundry Persons for Tender, money or deposits	325	Underwriting Commission	1,000
Application and Allotment Account	7	Purchase Account	1,075
Do. do. do.	110,850	Liquidator of old company	325
Call Account	73,900		<u>2,400</u>
	<u>£185,082</u>	Balance	182,682
			<u>£185,082</u>
Balance	182,682		
A/c.			
Purchase Account		Dr.	Cr.
Underwriting Commission		555,325	
Share Capital		1,000	
Cash		182,682	739,007
		<u>£739,007</u>	<u>£739,007</u>

The auditor, in the course of performing his duties, will proceed to check and agree the share transaction in the manner which has been outlined elsewhere. He should peruse carefully the Minutes of the Board, the Memorandum and Articles of Association of the company, and, in particular, the reconstruction agreements, seeing that the transactions are in accordance therewith, and that due effect has been given to the agreement.

AMALGAMATIONS.—In these days of world wide industrial upheaval and dislocation due to the effect of the Great War, amalgamations, fusions, absorptions, and consolidations (vertical and horizontal) among the various forms of combination in vogue have been and continue of common occurrence. Such changes invariably involve many matters of interest from the point of view of the subject of accounting and auditing, and the following simplified and condensed annotated examples may meet with acceptance. Condensed they are, since any attempt to discuss all the direct and circumlocutory detail and variations which arise in practice would be quite impracticable within the allotted space, and is moreover beyond the scope of the present article.

Let us assume the following data. The requisite resolutions are duly passed for the amalgamation of B Limited and C Limited with an existing company, A Limited. The amalgamation is to date from the 1st July, 19.., and at the

30th June of that year the following are the balance sheets of B Ltd. and C Ltd.

B Limited.			
	£		£
75,000 ordinary shares		Land and Works	50,000
£1 each	75,000	Goodwill	8,000
Debentures 5%	5,000	Debtors	13,000
Creditors	9,000	Bills Receivable	8,000
Bills Payable	9,000	Consumable Stores	7,000
Reserves	10,000	Stocks in Trade	18,000
Profit and Loss	6,000	Cash	10,000
	<u>£114,000</u>		<u>£114,000</u>

C Limited.			
	£		£
50,000 ordinary shares		Land and Works	75,000
£1 each	50,000	Debtors	15,000
50,000 5% Cum. Preference Shares of £1 each	50,000	Bills Receivable	5,000
Creditors	10,000	Materials and Stores	20,000
Works Pension Fund	15,000	Saleable Stocks	30,000
Depreciation Reserve	16,000	Cash	12,000
General Reserve	25,000	Profit and Loss for the Year	9,000
	<u>£166,000</u>		<u>£166,000</u>

The B and C Companies are to be voluntarily wound up, the A Co. taking over all the assets and liabilities of these entities. It is provided in the sale and purchase agreement *inter alia* that the shareholders and debenture holders in B Limited are to receive an equivalent holding in the A Company with a dividend of 2s. per share payable in cash free of tax and that the shareholders in B Limited are to receive a dividend of 10 per cent. for the year on the issued and paid up capital free of tax. The interest on the debentures in B Limited is payable half-yearly, viz., at the end of March and September. There are no dissentients. The liquidation expenses may be taken at £100 in each instance.

The directors of A are advised that in the case of B the value of the land and works is much in excess of £50,000.

It is decided to eliminate the item of goodwill and to regard any credit balance on the purchase account as a reserve towards income tax, etc.

The purchase account of B Limited in A's books will therefore be *pro forma*—

PURCHASE ACCOUNT.—B Limited.							
	£	s.	d.		£	s.	d.
To Share Capital				By Land and Works	50,500	0	0
Account—75,000 shares of £1 each	75,000	0	0	„ Debtors	13,000	0	0
„ 5% Debenture Holders	5,000	0	0	„ Bills Receivable	8,000	0	0
„ Bills Payable	9,000	0	0	„ Consumable Stores	7,000	0	0
„ Creditors	9,000	0	0	„ Stock in Trade	18,000	0	0
„ Sundry Debenture Holders for interest accrued at 30th June, 19..	62	10	0	„ Cash	2,500	0	0
„ Liquidator for Expenses	100	0	0				
„ Provision for Income Tax	837	10	0				
	<u>£99,000</u>	0	0		<u>£99,000</u>	0	0

Corresponding debits and credits will be made mostly by way of the Journal for the assets and

liabilities assumed in the foregoing purchase account. It may be noted that any amount paid by A Ltd. over and above £837 10s. 0d. for income tax in respect of B Ltd., as well as any other charges incurred incidental to or in connection with the acquisition of the undertaking, should be charged to the purchase account.

The account of C *pro forma* in A's books will similarly be as under—

PURCHASE ACCOUNT.—C Limited.							
	£				£		
To Share Capital A/c				Land and Works	59,000		
50,000 shares of £1 each	50,000			Debtors	15,000		
„ 50,000 Cum. Pref. shares	50,000			Bills Receivable	5,000		
„ Creditors	10,000			Materials and Stores	20,000		
„ Works Pension Fund	15,000			Saleable Stocks	30,000		
„ Reserve	9,750			Cash	5,750		
	<u>£134,750</u>				<u>£134,750</u>		

The Cash is composed of
 Less 10% on £50,000 = £5,000
 Preference Dividend, half-year 1,250
£6,250

and it is assumed that £5,750 is paid over to A.

It is decided to treat any credit balance in the purchase account as a reserve for income tax and any other matters to which it may be applied.

We need only give the *pro forma* journal entries for one of the instances. Those for C would be—

	£		£
Purchase Account	134,750		
To Ordinary Share Capital			50,000
„ Preference Share Capital			50,000
„ Sundry Creditors			10,000
„ Works Pension Fund			15,000
„ Reserve			9,750
For liabilities taken over in accordance with the terms of the sale and purchase agreement dated....			
Land and works			59,000
Debtors			15,000
Books Receivable			5,000
Materials and Stores			20,000
Saleable Stocks			30,000
Cash			5,750
To Purchase Account			134,750
For assets taken over in accordance with the terms of the sale and purchase agreement dated.....			

2. Assume the purchase by a company of an ordinary single venture for 20,000 fully paid shares of £1 each and £25,000 in cash, the debtors and creditors being for the account of the vendor.

The Assets acquired are valued by the purchasing company, and are—

Lands	£16,000
Plant and Machinery	13,000
Railways and Sidings	3,000
Buildings and Furniture	9,000
	<u>£41,000</u>

Here there is a debit difference of £4,000. Such a difference is sometimes implicitly created in

framing examination questions, the intention being that the examinee shall think of the solution by means of a goodwill account; but in practice that procedure is not always justifiable, and in the present case no goodwill was purchased, and though the figures given are supposititious the land was considered cheap, and it was decided to increase the lands account by the difference.

3. A new company, X Limited, has been formed with the object of acquiring and working the following and other similar businesses. The balance sheets of Y Limited and Z Limited are as under as at date of purchase—

Y Limited.			
	£		£
Share Capital—		Land and Works	16,000
24,000 shares of £1		Goodwill	2,000
each	24,000	Debtors	6,000
Creditors	6,000	Stock in Trade	5,000
Reserve	5,000	Stores and Materials	8,000
Profit and Loss	3,000	Cash	1,000
	<u>£38,000</u>		<u>£38,000</u>
Z Limited.			
	£		£
Share Capital—		Land and Works	17,000
29,000 shares of £1		Investments	2,000
each	29,000	Debtors	7,000
Creditors	6,000	Stock in Trade	3,000
Reserves	1,000	Stores and Materials	5,000
		Cash	1,000
		Profit and Loss	1,000
	<u>£36,000</u>		<u>£36,000</u>

The consideration in each case is the allotment in X Limited of fully paid shares equivalent to the amount of the assets indicated, less the liabilities to creditors, *i.e.* the net assets. Fractional rights are to be satisfied in cash, and Y and Z are to be wound up.

Assume the expenses of liquidation in each case £100.

The X Co. had already acquired 6,000 shares in Y Limited for £4,000, and sold them for £5,000.

Assume for the purpose of the illustration that there are no dissentients in the winding up of Z Limited, and no cash is required for the payment of fractional rights.

The Balance Sheet of X Limited at date is—

Authorised Capital—		Purchase of various interests, rights and options	
	£		£
1,000,000 shares of £1 each	1,000,000	Debtors	6,000
Capital issued—		Investments	4,000
60,000 shares of £1 each, 10s. paid	30,000	Cash at Bank, in hand, and on deposit	20,000
Creditors	5,000	Sundry Expenditure—less receipts	2,000
	<u>£35,000</u>		<u>£35,000</u>

In the case of Z we have

Less Profit and Loss	£1,000	£36,000
Creditors	6,000	
	<u>7,000</u>	
		<u>£29,000</u>

so that 29,000 shares of £1 each fully paid in X will be allotted to the shareholders of Z in cancellation of their present holdings in that company.

As to Y, we have—

	£38,000
Less Creditors	6,000
	<u>£32,000</u> and 32,000
	24,000 = 1½,

that is, shareholders in Y Limited will receive one share in X Ltd. and 6s. 8d. in cash for each share of their present holding.

At this stage let us prepare the following statement—

Shareholders of Y Limited nominal value of shares.	Holding in Y Limited.	Amount to which entitled in X Ltd. under the scheme.	Shares to be allotted	Fractions payable in cash.	Remarks
M	1,000	£ 1,333 6 8	1,333	0 6 8	
N	2,500	3,333 6 8	3,333	0 6 8	
O	1,300	1,733 6 8	1,733	0 6 8	
P	1,345	1,793 6 8	1,793	0 6 8	
Q	1,900	2,533 6 8	2,533	0 6 8	
R	675	900 0 0	900	—	
S	348	464 0 0	464	—	
T	254	338 13 4	338	0 13 4	
U	240	320 0 0	320	—	
V	135	180 0 0	180	—	
W	333	444 0 0	444	—	
X	8,000	10,666 13 4	10,666	0 13 4	
Y	5,370	7,160 0 0	7,160	—	
Z	600	800 0 0	800	—	
	<u>24,000</u>	<u>32,000 0 0</u>	<u>31,997</u>	<u>3 0 0</u>	M dissentients in legal form, and after negotiation his claim is settled for £600.

The purchase account of Y Ltd. in the books of X will be—

PURCHASE ACCOUNT.—Y Limited.

	£	s.	d.		£	s.	d.
To Share Capital				Land and Works	16,000	0	0
Account	30,664	0	0	Goodwill	2,000	0	0
„ Creditors	6,000	0	0	Debtors	6,000	0	0
„ Suspense	633	6	8	Stock in trade	5,000	0	0
				Stores and Materials	8,000	0	0
				Cash	297	6	8
	<u>£37,297</u>	<u>6</u>	<u>8</u>		<u>£37,297</u>	<u>6</u>	<u>8</u>

The cash is taken as under—

	£	s.	d.		£	s.	d.
Amount as per Balance sheet					1,000	0	0
Fractional payments							
Liquidation Expenses					2	13	4
Purchase of dissentients' rights					100	0	0
					600	0	0
					<u>702</u>	<u>13</u>	<u>4</u>
					<u>£297</u>	<u>6</u>	<u>8</u>

As there may be some small amounts not included in the Balance Sheet for which X will be liable, it is decided to create the suspense account indicated so that any relative payments may be charged thereto. In this connection X will be liable for any income tax, and should a liability be established payable in the ordinary course by Y it will fall on X, and should be debited to the purchase account. We now have the following statement from which we may prepare a Balance Sheet in the usual way, amalgamating the debtors, creditors, land and works, etc.

X LIMITED

[illegible]

	Z Ltd.	Y Ltd.		
	£	£	s.	d.
Land and Works	17,000	16,000	0	0
Goodwill		2,000	0	0
Investments	2,000		0	0
Debtors	7,000	6,000	0	0
Stock in Trade	3,000	5,000	0	0
Stores and Materials	5,000	8,000	0	0
Cash	900	297	6	8
	<hr/> 34,900			
Expenses of Liquidation	100			
	<hr/> 35,000	<hr/> 37,297	6	8
			72,297	6 8
Purchase of various Interests, rights and options		£ 6,000		
Debtors		4,000		
Investments		3,000		
Cash at bank, in hand, and on deposit		20,000		
Sundry Expenses, less receipts		2,000		
		<hr/> 35,000	0	0
		<hr/> £107,297	6	8

PURCHASE OF THE UNDERTAKING OF M LIMITED.

	£	s.	d.
To allotment of shares of 5s. each as per Board Minute dated, credited 4s. 6d. per share par. . .	50,000	0	0
" Sundry Creditors taken over	5,700	6	8
" Sundry petty cash payments on account of old Co. . .	53	17	6
" Sundry accounts of old Co. paid by new	50	8	5
	<u>£55,804</u>	<u>12</u>	<u>7</u>
To Balance	£36,984	16	8

Sundry debtors taken over	£	s.	d.
Cash Balances	6,000	0	0
Preliminary Expenses included in items as per contra—	564	7	6
Memorandum and Articles of Association	£150		
Fees in Deed Stamps	50		
Stamp Duty on Capital	750		
	<hr/>		
Investments of old Co. taken into account at market price	900	0	0
Amount received from Liquidators being the guaranteed dividend less tax on dissentients' interest purchased		50	18 4
Sundry receipts from Liquidators appropriated to purchase account		7	6 11
Profit on sale of investment		297	3 2
Remittance by Liquidators of old Co. to Colonial House in transit at date.		2,000	0 0
Balance		36,984	16 8
	<hr/>		
	£55,804	12	7

The reader may now contrast the foregoing accounts with the example above of a purchase account in the case of a reconstruction in which the scheme provides for a liability on the shares of the new company to which the shareholders in the reconstructed company are entitled.

It is assumed that the shares of the new company are of the denomination of 5s., credited 4s. 6d. per share paid. (See also CONVERSION OF PARTNERSHIP INTO A PRIVATE LIMITED COMPANY; CONVERSION OF A PRIVATE COMPANY INTO A PUBLIC COMPANY; DEBENTURES.)

LIMITED PARTNERSHIP.

(See AUDITING, p. 113; PARTNERSHIP ACCOUNTS
p. 768.)

LIMITED PARTNERSHIPS, AUDIT OF. (See AUDITING, p. 113.)

LINEAL CONSANGUINITY.

This is the relationship which subsists between persons each of whom is descended in a direct line from another, as between son, father, grandfather, great-grandfather, and so on in the direct ascending line, and between father, son, grandson, great-grandson, and so on, in the descending line. (See COLLATERAL CONSANGUINITY.)

LIQUID ASSETS.

Cash at the bank and in hand, and those assets which can be easily converted into cash.

LIQUIDATED DAMAGES.

These are the damages which are ascertained in amount, and the award or refusal of which depends entirely upon the question of liability pure and simple. Thus, if goods are sold and delivered, the price is ascertained at once; and, in an action to recover the price, the damages are what are known as liquidated. Again, if the parties to a contract agree as to the amount to be paid in case there is a breach of the contract, and the amount is not considered by the courts to be in the nature of a penalty, the damages are ascertained, or liquidated, and nothing more than the broad question of liability is to be considered. When a writ is specially indorsed and summary procedure is desired, this cannot be effected unless the damages are for a liquidated amount. (See UNLIQUIDATED DAMAGES.)

LIQUIDATION, COMPULSORY.

(See LIQUIDATORS, ACCOUNTS OF, p. 665.)

LIQUIDATION UNDER SUPERVISION.

(See LIQUIDATORS, ACCOUNTS OF, p. 665.)

LIQUIDATION, VOLUNTARY.

(See LIQUIDATORS, ACCOUNTS OF, p. 644.)

LIQUIDATORS, ACCOUNTS OF.

Liquidation is the method by which the affairs of a limited company are wound up. When for any reason it is considered desirable for the company to cease its business operations, it will be put into liquidation in one of the three forms prevailing, *i.e.* voluntary liquidation, liquidation under the supervision of the Court, liquidation under order of the Court.

The act of going into liquidation puts an end to the business transactions except in so far as further transactions may be necessary for the beneficial winding up of the company; but the liquidation itself is a more or less protracted state of affairs, during which the property of the company is ascertained and liquidated, and the rights thereto of the parties concerned determined.

The law under which companies are wound up is contained principally in Part 4 of the Companies (Consolidation) Act, 1908, and the Companies (Winding-up) Rules, 1909 and 1921.

AGENCY OF THE LIQUIDATOR.—The liquidator is in a somewhat different position from a trustee in bankruptcy, since although the object of his appointment is very analogous, there is the fundamental distinction that the property of the company does not vest in him as does the property of the bankrupt in his trustee.

The liquidator is an agent, and as such is, quite apart from the Statute or Rules, under a duty to keep proper and correct accounts, which he must be ready to produce, together with the books and documents in his hands, at all times. He must keep the money and property of his principal separate and distinct from his own money, or from that of other persons which may be in his hands, and he must pay over in a proper manner such money from time to time.

It will be shown, however, that quite apart from these principles of common law, the Companies (Consolidation) Act and the Rules made thereunder necessitate the keeping of proper accounts in every liquidation, and particularly in a liquidation carried out under the order of the Court.

VOLUNTARY LIQUIDATION.—(a) **Appointment of Liquidator.** In voluntary liquidation the winding up is entirely in the hands of the liquidator of the company except so far as restrictions are imposed by the Companies (Consolidation) Act or by the Court on application; *e.g.* under Section 214 an extraordinary resolution of the company must be obtained for the sanction of compromises; under Section 192 a special

resolution is required to enable the liquidator to sell the assets of the company for shares in another company; under Section 193 any creditor or contributory may apply to the Court to control the liquidator.

Apart from such examples the liquidator has the conduct of the winding up in his own hands, and can safely exercise his discretion so long as he complies with the law relating to the duties he has undertaken.

The liquidator will be appointed generally by the company in general meeting, and the appointment may be made in the same resolution as that by which the company is put into liquidation.

The company may, however, by extraordinary resolution, delegate the power of appointment of liquidator to the creditors, or if no liquidator is appointed the Court may appoint a fit and proper person upon the application of any contributory.

The liquidator must file notice of his appointment with the Registrar of Companies within twenty-one days of appointment under a penalty of £5 a day for default.

Upon the liquidator's appointment a meeting of creditors must be summoned by him by seven days' notice sent within seven days of appointment, and must be held not less than fourteen nor more than twenty-one days after appointment, being advertised once in the *Gazette* and once in two local newspapers. General and special forms of proxy must be enclosed with the notices posted to the creditors (Rule 141). The object of the meeting is to enable the creditors to decide whether or not they will apply to the Court for the appointment of a substitutional or joint liquidator or for a Committee of Inspection, and if the meeting decides to do so it may appoint some creditor to make the application, and he must make it not later than fourteen days from the date of the meeting.

The Court may order the removal of the liquidator appointed by the company and appoint another, or may appoint a joint liquidator, or may appoint a committee, and may make an order as to costs.

The appointment of the liquidator must be gazetted, and production of the *Gazette* containing the resolution is accepted as evidence of the appointment. A copy of any resolution passed at the meeting must also be filed with the Registrar (Rule 129) and minutes of the meeting must also be entered in a book kept for the purpose (Rule 139).

(b) **The Liquidator's Accounts.** In the case of a voluntary liquidation there are no Statutory enactments relating to the keeping of accounts, except the provisions of Section 224 of the Act and the Rules made thereunder. It is obvious, however, that a liquidator in voluntary liquidation must keep accounts, and moreover he should be a person with a fair and adequate understanding of the principles upon which accounts are compiled.

The knowledge of accounts is necessary, not so much by reason of the accounts that he has to keep, but rather that he may understand the accounts which he has to examine when he enters upon his duties.

(c) **Section 224 of the Companies (Consolidation) Act, 1908.** In any liquidation, whether compulsory, voluntary or under supervision, if not concluded within one year, the liquidator must send to the Registrar of Joint Stock Companies a statement of account dated from the last statement, in duplicate, twice each year; the first at the expiration of thirty days from the end of the first year during which the liquidation proceedings have been pending, and the succeeding statements at intervals of half-a-year, until the winding up is concluded.

Where a business has been carried on, a Trading Account must also be sent as a distinct account, and the totals entered in the principal statement.

Any creditor or contributory, stating himself in writing to be such, may inspect and take a copy of, or extract from, such statement. If the liquidator makes default, the penalty is £50 a day. The Board of Trade may extend the time in any particular case for special reasons; and may direct other intervals than those above stated.

The account must be verified by affidavit, and the Board of Trade may direct and enforce an audit of the account. Where there have been no receipts and payments during the period the liquidator must submit an affidavit to this effect.

For the purpose of Section 224, the winding-up of a company is deemed to be concluded—

(a) In case of companies wound up by the Court, at the date on which the order dissolving the company has been reported by the Official Receiver to the Registrar of Joint Stock Companies (as a matter of practice this is not done till at least two years after the making of the order); or at the date of the order of the Board of Trade releasing the liquidator under Section 157.

(b) In case of companies wound up voluntarily, or under the supervision of the Court, at the date of the dissolution of the company, unless at such date any funds or assets of the company remain in the hands or under the control of the liquidator, in which case the winding-up is not deemed to be concluded until such funds or assets have been either distributed or paid into the Companies Liquidation Account at the Bank of England. (R. 188, 191.)

After dissolution the Court may, on application, declare the dissolution void at any time within two years.

The person applying must file an office copy of the order with the Registrar within seven days. Penalty for default, £5 a day. (Section 223 (2).)

If from such statement rendered under Section 224, it appears that the liquidator has in his hands

any money representing unclaimed or undistributed dividends or assets of the company, which have remained undistributed for six months after the date of receipt, he must forthwith pay the same to the Companies Liquidation Account at the Bank of England, and is entitled to a receipt and certificate discharging him in respect thereof. Application must be made to the Board of Trade for a paying-in order. (R. 191 (4).)

Immediately on the conclusion of the liquidation, even if it be concluded within one year, these unclaimed dividends and undistributed assets are to be paid into the Companies Liquidation Account. (R. 191 (3).)

Any person claiming the money may apply to the Board of Trade, which, on certification by the liquidator that such person is entitled, makes an order for payment to him; subject to appeal to the High Court.

For the purpose of ascertaining whether these amounts are correct, the Board of Trade may require the return under Section 224 to be made, even if the liquidation be completed within one year, but this is not usually required in voluntary liquidation.

The forms of account prescribed under the Rules are given on pages 646 and 647.

Upon receiving the return made under Section 224 the Registrar will call upon the liquidator to pay into the Companies Liquidation Account all unclaimed dividends or undistributed assets of the company which have remained undistributed for six months after the date of receipt. If there are no unclaimed dividends, but a cash balance has been in hand during the period covered by the return, the Registrar will require the minimum balance in hand during the period to be forthwith paid into the Companies Liquidation Account.

In order to make payments into the Companies Liquidation Account a receivable order must be applied for and the necessary particulars entered on the application therefor and upon the receivable order itself, after which the money will be accepted by the Bank of England. Even if the money is on deposit and so earning interest, the Registrar will require sums which ought to be paid into the Companies Liquidation Account to be forthwith paid in, though no interest will be allowed upon such moneys after they are so dealt with.

The liquidator is entitled to a receipt and certificate discharging him in respect of moneys paid into the Companies Liquidation Account. Any such money paid into the Account, which is subsequently required, will be paid out on a certificate by the liquidator that such person is entitled thereto, subject to an appeal to the High Court.

(d) **The Accounts of the Company.** The liquidator, upon appointment, should complete the accounts of the company and ascertain as far as possible that they are correct. The object of

NOTE.—The liquidator should also state—

- | | | | | | | |
|---|---|---|------------------------|---------|---------|---------|
| (1) The amount of the estimated assets and liabilities at the date of the commencement of the winding-up. | { | Assets (after deducting amounts charged to secured creditors and debenture holders) | .. .. . | .. .. . | .. .. . | .. .. . |
| | { | Liabilities | .. { Secured creditors | .. .. . | .. .. . | .. .. . |
| | | | Debtenture holders | .. .. . | .. .. . | .. .. . |
| | | | Unsecured creditors | .. .. . | .. .. . | .. .. . |

- | | | | | | |
|--|---|-------------------|-----------|----|---|
| (2) The total amount of the capital paid up at the date of the commencement of the winding-up. | } | Paid up in cash.. | .. | .. | £ |
| | | Issued as paid up | otherwise | | |
| | | than for cash | .. | .. | £ |

- (3) The general description and estimated value of outstanding assets (if any). }

- (4) The causes which delay the termination of the winding-up.

- (3) The period within which the winding-up may probably be completed.

No. of Company

No. 93. (Rules 189 and 190.)

AFFIDAVIT VERIFYING STATEMENT OF LIQUIDATOR'S ACCOUNT UNDER SECTION 224.

(Name of Company.)

I,
of
the liquidator of the above-named Company, make oath and say: That **the account hereunto annexed marked B contains a full and true account of my receipts and payments in the winding-up of the above-named Company, from the day of 19 , to the day of 19 , inclusive, *and that I have not, nor has any other person by my order or for my use during such period, received or paid any moneys on account of the said Company, *other than and except the items mentioned and specified in the said account.*

I further say that the particulars given in the annexed Form 92, marked B, with respect to the proceedings in and position of the liquidation, are true to the best of my knowledge and belief.

Sworn at

* NOTE.—If no receipts or payments, strike out the words in italics.

The affidavit is *not* required in Duplicate, but it must in every case be accompanied by a statement on Form 92 in duplicate.

doing this is to enable him to ascertain full particulars of the assets and liabilities of the company as shown by the books. This is a matter of paramount importance, since the rights of creditors and of shareholders depend upon the actual amounts due to or contributed by them; while those rights can only be discharged out of the proceeds of the assets of the company, which must be ascertained before they can be dealt with.

(e) **Statement of Affairs.** It will not always happen that a Statement of Affairs has been prepared in respect of a company which has gone into voluntary liquidation, though it is usual where the cause of the winding-up is the fact that the company is unable to pay its debts. Where a Statement of Affairs is in existence, this will no doubt have been prepared by a professional accountant, possibly by the auditor of the company, and should, in such a case, give very valuable information as to the state of the company's affairs at the time when it goes into liquidation.

Upon completing the accounts of the company it is desirable to agree them with the Statement of Affairs, and for this reason the accountant who prepared it should be asked for a copy of the Trial Balance upon which it is based.

It is very important to do this, since if any discrepancy exists between the books and the Statement of Affairs it is important to have it brought to light at the earliest possible moment.

The liquidator must remember that the creditors and contributories will judge the result of the liquidation very largely by the position of affairs shown on the statement presented to them at the time the liquidation is entered into.

(f) **Distinction between the Accounts of the Liquidator and the Company.** The accounts of the liquidator must be kept quite distinct from the accounts of the company. It has been shown that it is desirable for the liquidator to complete the accounts of the company and, if possible, to reconcile therewith the Statement of Affairs, if any, which has been presented. Having done this, however, it is not desirable that the liquidator should continue the accounts of the company.

It is not, of course, necessary that new ledgers should be opened in full, but it is desirable that the liquidator should have separate books and that the balances should all be transferred into his own books as liquidator. The easiest method of dealing with this will be shown later.

The books required by the liquidator for the purpose of keeping his accounts will be—

- The Cash Book;
- The Ledger;
- The Minute Book;
- Register of Debtors;
- Register of Creditors.

The whole of the balances should be transferred out of the books of the company into the books

of the liquidator, but in such a way that the minimum amount of labour will be involved.

It will be understood that these remarks apply only to the financial books of the company and have no reference to the statistical books.

(g) **The Realisation of Assets.** The liquidator's duty is to obtain control of all the assets and turn them into money; the only exception being such a case as reconstruction, where the assets are transferred to another company for shares in that other company.

(1) **BOOK DEBTS.** The Register of Debtors, to which reference has already been made, should be written up with the agreed balances in the trade ledgers of the company. The register should show the amount at the debit of each debtor; the date or dates when cash is paid or amounts allowed; and columns to record cash received, discount allowed, and allowances other than discount. The date of applications for payment and remarks in respect of any item (*e.g.* placed with solicitor) should be entered in the "Remarks" column.

On the next page is a form of this register with specimen entries, which should be found self-explanatory.

(2) **STOCK-IN-TRADE.** If a Statement of Affairs is prepared at the date of the company going into liquidation, there will doubtless be stock sheets in existence containing an inventory of the stock and valuations placed upon each item. This should be checked by the liquidator, if possible, upon taking possession of the company's assets.

If no stock sheets are in existence, it is extremely desirable that the liquidator should make an inventory of the stock as he finds it on taking possession, since it is only by having this information *ab initio* that he can properly control the realisation of this asset.

The liquidator may sell off the stock piecemeal, in which case it is desirable to record on the stock sheets or stock inventory the detailed amounts realised. If the stock is sold by an auctioneer, the marked catalogue will usually be provided by him as a voucher for the proceeds of sale. Even if the sale of the stock is carried through in one transaction by private arrangement, it is desirable to have this inventory prepared, as otherwise the liquidator cannot be in a position to judge whether the contract which he makes is or is not for the benefit of the liquidation.

The liquidator, when selling stock in this way, should always endeavour to obtain some voucher which will enable him to produce evidence in support of the amount for which he accounts. This is a wise business precaution, since, although the accounts of a liquidator in a voluntary liquidation are not subject to any official audit, the liquidator may nevertheless be called upon to substantiate his return under Section 224, in respect of which the Board of Trade may enforce an audit.

REGISTER OF DEBTORS

Regis- tered No.	Sales Ledger Folio.	NAME.	Amount of Debt.		Date.	Cash Book Folio.	Cash.		Discount.		Allowance.		Remarks.
			£	s.	d.		£	s.	£	s.	£	s.	
263	109	Newcastle-on-Tyne Wire Works, Newcastle				19..							
264	765	Nicholls, Ltd., Taunton..	110	14	4	Dec. 10	1	10	0				
265	342	Northern Electric Manufacturing Co., Ltd., 416 High Street, Glasgow..	5	16	7	Nov. 8 19..	1	3	7	5	10	9	
						Mar. 4	3						In Liqd. See letter from Lewis Owen & Co. (13/4 in £). Returns.
266	214	Non-rustable Tin Co., Ltd., Romford..	8	10	0	April 9	3	12	0	8	0	0	
267	132	Naughton & Co., Clarence Road, Whitby..		19	10	" 16	3	19	10				
268	542	Natterson Music Hall, Natterson ..	25	0	0	June 4	4	0	0				
269	423	Owen & Co., Ltd., Lloyd St., Portsmouth..	2	18	2								Letters returned marked "Gone Away."
270	165	Odell, Thomas, 132 Broad Street, Exeter..	52	7	4	19..	1	0	0		7	4	See
271	5	Orton & Co., The Parade, Margate ..	376	16	6	Dec. 10	1	52	0	18	16	9	Correspond- ence
272	67	Palmer & Patterson, 4 Acre Lane, Hull ..	27	14	3	Oct. 10	1	357	19	9			Contra Account. Difference on Invoice.
273	152	Picture Palaces, Ltd., London Road, E ..	1	6	10						1	6	Invoice entered twice.
274	97	Portford & Co., Broadway, Halford ..	12		6	19..	2	12	6				
275	512	Pecker, Frank, Turnstile Street, Ashford ..	10	0	0	Jan. 27					10	0	0
276	2	Rayner, Ltd., Ramsgate ..	540	10	6	July 4	4	15	9		9	14	9
277	85	Retford, Alan, Mile End Road, E. ..	1	3	0								Returns not credited. Receiving Order made 20th Dec. 19..
278	418	Robbins & Curtis, Garrison Road, E.C. ..	32	17	9	Jan. 8	2	17	9				No Assets. First & Final Div.
279	13	Retts, Ltd., Spring Gardens, Dublin ..	56	18	2			4	6				5/- in the £. See Correspond- ence from solicitors.
280	63	Russell Bros., Port Street, Buxton ..	9	5	0								Agreed to pay £10 a month.
281	31	Roberts, F., 120 Weston Road, Hampstead	35	15	0	19..	1	0	0				
						Nov. 10	1	10	0				
						Dec. 10	1	10	0				
						1914.	2	10	0				
						Jan. 11	3	5	15				
						Feb. 10							

(3) **PLANT AND MACHINERY.** Plant and machinery will generally be found to stand at one figure in the Plant and Machinery Account in the books of the company. This figure should be transferred to a Plant and Machinery Account in the liquidator's ledger, so that a record will be kept of it in his books.

It will generally be found that, although one balance may represent this asset in the accounts, it will, in fact, consist of a number of separate items, such as machines, utensils, etc.; and it is, therefore, very desirable that an inventory should be made of these when the liquidator takes possession of the assets. If these are then sold, either piecemeal or as a whole, whether at auction or privately, it can be shown in the same way as in connection with the stock how the proceeds have been accounted for.

(4) **REAL PROPERTY.** The balance of freehold or leasehold property account will be entered into the liquidator's ledger, and a memorandum made thereunder showing of what the property actually consists and describing it with a sufficiency of detail.

The gross proceeds of the realisation of this and similar assets should be entered as a receipt, the expenses of sale being shown as a payment.

(5) **BILLS RECEIVABLE.** The balance of Bills Receivable Account should be entered in the liquidator's ledger and a detailed inventory of the bills also shown. As such bills mature they should be collected and the proceeds accounted for.

(6) **GOODWILL.** The balance standing to the Goodwill Account, if any, should be entered in the liquidator's ledger, although in many cases it may prove to be a worthless asset; while on the other hand if no goodwill appears in the books it is possible that there may still be a saleable goodwill passing through the liquidator, which it is his duty to dispose of for the company's advantage.

The liquidator must therefore carefully consider the question of goodwill, which in no way depends upon entries in the books or book values, and if he finds that any advantage attaches to the business connection of the company, he should use his utmost endeavours to sell it for the best price obtainable.

(7) **CARRYING ON THE BUSINESS.** Where a goodwill does exist it may be necessary and desirable for the liquidator to carry on the business until such time as he can sell it entirely as a going concern. For this purpose in voluntary liquidation he should obtain an indemnity from the persons who will benefit from the continuance of the business, since if he incurs liabilities he will be personally responsible for payment if the assets of the company have proved insufficient.

The Act only contemplates the business being

carried on with a view to the beneficial winding-up, and the liquidator must therefore not carry it on indefinitely.

Where the liquidator does carry on trading he should, where possible, sell for cash only, and for his own protection he should buy on the same terms. A separate account should be kept of the receipts and payments relating to the trading, and the totals of this should be incorporated weekly in the General Cash Book.

Even if the transactions are not entirely cash transactions it is still desirable to keep a separate record of the trading receipts and payments so that these can be entered in the general Cash Book in weekly totals. Where credit is taken or given the fact must be recorded in the liquidator's books in the usual manner.

(8) **RECOVERY OF INCOME TAX.** An important matter in connection with the realisation of assets is the question of income tax. Under the Income Tax Act, 1918 (Rule 8, §2), where a profession, trade or vocation is discontinued in any year, there is a right to be charged on the actual amount of profit or gain arising in that year; and if the person concerned can prove to the satisfaction of the Commissioners that the total amount of income tax paid during the three previous years in respect of the trade, etc., exceeds the total amount which would have been paid if he had been assessed in each of those years on the actual amount of the profits, he is entitled to repayment of the excess. This section applies to companies also, and the liquidator should therefore examine the Profit and Loss Accounts for the current year, and for the three previous years, and compare the adjusted results thereof with the amount of income tax actually paid.

If profits have declined it will clearly be his duty to reclaim a certain amount of tax under this section.

(h) **Uncalled Capital.** The uncalled capital of the company may be available as assets in the liquidator's hands. For instance, if there are insufficient assets otherwise to pay all the liabilities of the company, and some or all of the shares are only partly paid, the creditors have a right to the balance of the uncalled capital so far as it is necessary to repay them in full, and it will therefore be the duty of the liquidator to make such a call as will be sufficient for this purpose.

It may also be necessary for the liquidator to call up unpaid capital on ordinary shares in order to repay to the holders of the preference shares the amount due to them in respect of a preference as to capital, and it may even be necessary to call up unpaid capital where there is only one class of shares, when they are not all paid up to the same extent. In such a case the liquidator will have to adjust the rights of the shareholders

inter se, and if there is no surplus of assets otherwise available, it could be done by calling up, in respect of those shares showing the smallest amount paid, a sum sufficient to make all the shares equally paid, and then distributing the proceeds *pari passu*. The adjustment can, of course, be made before the amount is called up so that only the actual net sum required should be called for, but in this case allowance must be made for any calls that may not be recoverable.

When the necessity for making a call arises the liquidator must settle the list of contributories.

The liquidator has full power to settle the list of contributories, and any list settled by the liquidator on his own responsibility is *prima facie* evidence of the liability of the persons named therein to be contributories. (Section 186 (6).)

Notice to the contributories of an appointment to settle the list is not absolutely necessary, though it is advisable that it should be given.

The liquidator can rectify the register, or sanction transfers of shares, without leave of the Court.

In one sense the term "contributories" includes all members of the company, but for the purpose of settling the list it may be limited to those whose shares are not fully paid.

There are two lists—the "A" and the "B" lists. The "A" list includes all those who were members of the company at the date of the winding-up, and each member is liable for the balance remaining unpaid on his shares. The "B" list includes all persons who, though not members at the date of winding-up, have held shares at any time within a year previous to the winding-up. The liability of these "B" contributories is doubly limited. Each "B" contributory is only liable for such portion of the balance due on his shares as is not paid by his "A" contributory, and only for such portion of that amount as is required to pay debts which existed before he ceased to be a member.

The liquidator cannot call upon any "B" contributory till he has exhausted the whole of the "A" list; and then, if still in need of funds, he may call on any or all of the "B" contributories for the amounts for which they are liable; but each "B" contributory, when called upon, can require the liquidator to "marshal the debts"—that is to say, to show that the debts in respect of which he is required to contribute existed before he ceased to be a member.

All moneys contributed by "B" contributories form part of the general assets, and are not utilised solely for payment of creditors in respect of whose debts they are contributed. (*Webb v. Whiffen*, 1871, *L.R.*, 5 *H.L.*, 711.)

Illustration. The company being in liquidation and the ordinary shares being 10s. paid, the

liquidator called up the remaining balance on the shares.

A, a contributory holding 100 shares 10s. paid, and B, a contributory holding twenty-five shares 10s. paid, are unable to contribute the amounts due from them.

A had taken a transfer of his shares from X three months before the commencement of the liquidation, and B had acquired his shares from Y six months before the commencement of the liquidation. Of the liabilities existing at the commencement of the liquidation, £10 was owing to F six months prior to the liquidation, and £60 was owing to G three months prior to the liquidation. How much can be called up from X and Y, and what will be done with the proceeds?

X and Y being "B" contributories are only liable to the extent of debts remaining unpaid which existed when they were members of the company. Y's outside liability was £12 10s., *i.e.* 10s. per share on twenty-five shares, but as only £10 remains unpaid in respect of liabilities existing when he was a member he can only be called upon to pay up the sum of £10. In the case of X his utmost liability is the amount remaining unpaid on the shares, *i.e.* £50, and as the debts which existed when he was a member exceed this sum, he must pay up in full the balance on his shares.

The proceeds of the calls made on these "B" contributories will not be utilised for the benefit of F and G, but will go to the common fund for the benefit of all the creditors.

With regard to the form of the list of contributories, there is nothing prescribed with regard to voluntary liquidations, but the form prescribed in compulsory liquidations can be used.

The form prescribed for compulsory liquidation is given on the next page.

(j) **Record of Receipts and Payments.** As there are no prescribed books the liquidator can keep the Cash Book in such form as he chooses. As the account to be presented is an account of receipts and payments it will be necessary, if the ordinary form of Cash Book is used, to analyse it periodically in order that the accounts to be submitted may be correctly shown.

The Cash Book should be written up from day to day so that information as to the cash position is always available.

When trading is carried on, a separate Cash Book should be utilised for recording the receipts and payments on Trading Account; and the totals of such receipts and payments should be transferred to the principal Cash Book each week.

(k) **Bank Account.** The liquidator must open a separate account in his official name as liquidator of the company, and all moneys received should be paid into this account, and all payments made by him should be made by cheque drawn upon it.

FORM No. 42. (Rule 77.)

PROVISIONAL LIST OF CONTRIBUTORIES TO BE MADE OUT BY LIQUIDATOR

(Title.)

The following is a list of members of the Company liable to be placed on the list of contributories of the said Company, made out by me from the books and papers of the said Company, together with their respective addresses and the number of shares [or extent of interest] to be attributed to each, so far as I have been able to make out or ascertain the same.

In the first part of the list, the persons who are contributories in their own right are distinguished.

In the second part of the said list, the persons who are contributories as being representatives of, or being liable to the debts of others, are distinguished.

FIRST PART.—CONTRIBUTORIES IN THEIR OWN RIGHT

Serial No.	Name.	Address.	Description.	Number of Shares [or extent of Interest].

SECOND PART.—CONTRIBUTORIES AS BEING REPRESENTATIVES OF, OR LIABLE TO THE DEBTS OF, OTHERS

Serial No.	Name.	Address.	Description.	In what Character included.	Number of Shares [or extent of Interest].

He must not pay money into his own private account, though he will have just as effective a control over money paid into the special account as if he had paid it into his private account, but the fact that he is an agent necessitates the separation of the money coming to him as liquidator from any other private or business money.

The Bank Pass Book should be agreed with the Cash Book periodically, and if a considerable balance is retained at the bank it should be placed on deposit so as to be earning interest during the time that it would otherwise be lying idle.

(l) **Payments by the Liquidator.** The liquidator must apply the assets received by him in discharge of the costs of the liquidation and his own remuneration, and in payment of the liabilities of the company in their proper order.

The order in which these various payments should be made is as follows—

- (a) Secured creditors out of their securities.
- (b) Costs and remuneration.
- (c) Preferential creditors.
- (d) Unsecured creditors.
- (e) Payments to contributories in accordance with their rights and interests.

(m) **Secured Creditors.** Where a creditor holds security greater in value than the amount of his debt, the liquidator should at once redeem the security by paying out the debt in full. This will have the effect of preventing interest running against the estate, and securing the property for the advantage of the liquidation.

Where the security is less than the amount of the debt the rights of the parties will depend primarily upon the exact contract made at the time when the security was lodged. Generally, it will be found that the person who has lent money on security has a right to sell the security and pay himself out of the proceeds; and to the extent to which the proceeds of the security do not repay him he will be able to claim in liquidation.

It should be noted that interest is not stopped from running against the estate in the case of voluntary liquidation unless the company is insolvent (*re Thos. Salt & Co.*, 1908, 98 L.T. 558); but even if the company is insolvent a fully secured creditor can always get his interest out of his security.

(n) **Debentures.** Debenture-holders are secured creditors and will rank for payment before either the preferential creditors or the ordinary unsecured creditors. They will also rank in priority to the liquidator of the company so far as his remuneration and costs of liquidation are concerned, for which reason it is very necessary that the liquidator before entering on the liquidation should come to an understanding with the debenture holders to pay his remuneration and costs.

Where the debentures are secured by a floating

charge only, preferential creditors must be paid in priority to the debenture holders though the latter are entitled to be recouped as far as may be out of any assets of the company available for the payment of general creditors.

It must be borne in mind that debenture holders are only secured against the liquidator or any creditor of the company if the debentures are registered with the Registrar of Companies within twenty-one days of creation, and it is important, therefore, that the liquidator should, before treating the claims of such debenture holders as secured, see that the registration has been properly carried out within the required time, and that the debentures themselves are *intra vires* the company.

(o) **Costs and Remuneration.** Section 196 of the Companies (Consolidation) Act, 1908, provides that all costs, charges and expenses properly incurred in the winding up of a company including the remuneration of the liquidator shall be payable out of the assets of the company in priority to all other claims.

The remuneration of the liquidator may take the form of a percentage on realisation, or on realisation and distribution; or the liquidator may agree to perform the necessary work in consideration of a lump sum. The remuneration is fixed by the company, but if not so fixed the liquidator may apply to the Court to fix it.

It may happen that the assets available for the liquidator may be insufficient to pay the costs of the winding-up and the liquidator's remuneration, and where this is so the liquidator should, for his own sake, get a guarantee for his remuneration either from the directors or from those persons who are interested in the winding-up. If this is not done he will have no remedy for the amount due to him which is not covered by the assets. In such a case if recourse has to be had to the guarantee this will form no part of the assets of the liquidation and need not be brought into account in connection therewith.

(p) **Preferential Creditors.** Section 209 of the Companies (Consolidation) Act provides that—

"(1) In a winding up there shall be paid in priority to all other debts—

"(a) All parochial or other local rates due from the company at the date hereinafter mentioned, and having become due and payable within twelve months next before that date, and all assessed taxes, land tax, property or income tax assessed on the company up to the 5th day of April next before that date, and not exceeding in the whole one year's assessment;

"(b) All wages or salary of any clerk or servant in respect of services rendered to the company during four months before the said date, not exceeding £50; and

"(c) All wages of any workman or labourer not exceeding £25, whether payable for time or for piece work, in respect of services rendered to the company during two months before the said date; Provided that where any labourer in husbandry has entered into a contract for the payment of a portion of his wages in a lump sum at the end of the year of hiring, he shall have priority in respect of the whole of such sum, or a part thereof, as the Court may decide to be due under the contract, proportionate to the time of service up to the said date; and

"(d) Unless the company is being wound up voluntarily merely for the purposes of reconstruction or of amalgamation with another company, all amounts (not exceeding in any individual case, £100) due in respect of compensation under the Workmen's Compensation Act, 1906, the liability whereof accrued before the said date, subject nevertheless to the provisions of Section 5 of that Act.

"(2) The foregoing debts shall—

"(a) Rank equally among themselves and be paid in full, unless the assets are insufficient to meet them, in which case they shall abate in equal proportions; and

"(b) In the case of a company registered in England or Ireland, so far as the assets of the company available for payment of general creditors are insufficient to meet them, have priority over the claims of holders of debentures under any floating charge created by the company, and be paid accordingly out of any property comprised in or subject to that charge.

"(3) Subject to the retention of such sums as may be necessary for the costs and expenses of the winding-up, the foregoing debts shall be discharged forthwith so far as the assets are sufficient to meet them.

"(4) In the event of a landlord or other person distraining or having distrained on any goods or effects of the company within three months next before the date of a winding-up order, the debts to which priority is given by this section shall be a first charge on the goods or effects so distrained on, or the proceeds of the sale thereof:

"Provided that in respect of any money paid under any such charge, the landlord or other person shall have the same rights of priority as the person to whom the payment is made."

In the case of a voluntary winding-up, these debts are preferential up to the date of the commencement of the winding-up (*i.e.* the date of the resolution), or, in the case of a special resolution, the date of the confirmatory resolution.

Under the National Insurance Act, 1911, contributions payable by the employer in respect of the employed contributors or workmen in an assured trade during the four months, before the commencement of the winding-up are also preferential, unless the company is being wound up voluntarily for the purpose of reconstruction or amalgamation.

Since the Crown is not expressly bound by the order of priority of debts under the Companies (Consolidation) Act, 1908, as is the case under the Bankruptcy Acts, the Crown, whether preferential or not, may claim to be paid in full in priority to all other unsecured creditors (*re Oriental Bank*, 28 C.D. 643).

Where a winding-up order is made prior to the 1st December in the year of assessment, the Inland Revenue authorities will make no claim on the Official Receiver or liquidator for income tax (Schedule A), inhabited house duty, and land tax for the year ending 5th April next following the date of the winding-up order, unless the Official Receiver or the liquidator remains in possession of the premises until the following 1st January.

With regard to the wages or salary of a clerk or servant, it has been decided that commission is preferential (*re Klein*, 1906, W.N. 148); and that opera singers are servants (*re Wintergarten German Opera*, 1907, 23 T.L.R. 662). A managing director, however, is not a clerk nor a servant, and is, therefore, not preferential (*re Newspaper Proprietary Syndicate, Ltd.*, 1900, 2 Ch. 349).

A secretary is only preferential if he is the servant of the company, that is, if his secretarialship is his sole employment; a person who acts as secretary to two or more companies is not preferential in any of them (*Cairney v. Back*, 1906, 2 K.B. 746).

So far as workmen are concerned, if they are paid partly by wage and partly by commission on the work turned out, the commission is as much preferential as the wages (*re Earle's Shipbuilding, etc., Co.*, 1901, W.N. 78).

As an illustration of the effects of the clauses relating to salary and wages, the case of a clerk may be taken whose salary is at the rate of £300 per annum. If his salary were two months in arrear, the whole amount due to him of £50 would be preferential; but if it were three months in arrear, £50 would be preferential, and for the remaining £25 he would have to rank as an ordinary unsecured creditor.

The liquidator is not required to pay out the preferential debts in priority to the costs and his own remuneration, since these are payable out of the assets of the company in priority to all other claims under Section 196 of the Act. The preferential claims, as already shown, may rank in priority to the rights of debenture holders under a floating charge.

(g) **Unsecured Creditors.** The liquidator should prepare a register of creditors existing at the date of the liquidation, agreeing the same with the books of the company. All doubtful items should be enquired into and settled as soon as possible, the creditors being required to give such information as the liquidator may think necessary to enable him to determine whether or not he shall admit the claim made.

The liquidator may fix a certain day, not less than fourteen days from the date of the notice, on or before which the creditors are to prove their debts or claims, or to be excluded from the benefit of any distribution made before such debt is proved. Notice is to be given by advertisement in such paper as the liquidator shall think convenient, and to the last known address of each person who, to the knowledge of the liquidator, claims to be a creditor, and whose claim has not been admitted.

It should be observed that there is not, strictly speaking, a proof in these cases; there is only a claim which the liquidator may require to be verified by statutory declaration. If the liquidator refuses to pay any claim, the creditor may sue.

In view of the fact that the company may prove to be insolvent, the rules of bankruptcy as to proof should be strictly adhered to.

The date to which interest should be included, or at which set-off should be taken, is the commencement of the liquidation.

Under certain circumstances, however, proofs can be called for, but this is only where there is a probability that there will be several disputed claims, in which case the liquidator may, in order to avoid liability, apply for an order as to the creditors of the company. The liquidator in this case must—

1. Advertise for claims to be sent in.
2. Investigate debts and claims.
3. Leave at the Registrar's Chambers a list of all claims, distinguishing between those which he considers due, and those which ought to be proved.
4. File an affidavit stating which debts and claims are in his opinion justly due, and the reason for his belief.
5. Give notice to creditors whose debts have been allowed; and call upon others to come in and prove on a day named, not less than four days from date of notice.

The result of adjudication on debts and claims is stated in a certificate made by the master.

On the next page is a form of Register of Creditors, from which can be seen the general method of keeping accounts in connection with the liabilities of the company.

By Section 206 of the Companies (Consolidation) Act, it is provided that all debts payable on a contingency, and all claims against the company,

present or future, certain or contingent, ascertained or sounding only in damages, shall be admissible to proof against the company, a just estimate being made so far as possible of the value of such debts or claims as may be subject to any contingency or sound only in damages, or for some other reason do not bear a certain value. This provision only applies where the company is able to pay all its debts; but where it is insolvent, the provisions of Section 207 of the Act will apply. Every company in liquidation is deemed to be insolvent until it is shown that the assets are sufficient to pay the debts in full (*Milan Tramways Co.*, 1884, 25 Ch. 587).

Under Section 207 of the Act, it is provided that in the winding-up of an insolvent company registered in England or Ireland, the same rules shall prevail and be observed with regard to the respective rights of secured and unsecured creditors, and to debts provable, and to the valuation of annuities and future and contingent liabilities as are in force for the time being under the law of bankruptcy in England or Ireland, as the case may be, with respect to the estates of persons adjudged bankrupt; and all persons who, in any such case, would be entitled to prove for and receive dividends out of the assets of the company, may come in under the winding-up and make such claims against the company as they respectively are entitled to by virtue of this section.

The Bankruptcy Rules as to the rights of secured and unsecured creditors, as to debts and liabilities provable, and as to the valuation of annuities and future and contingent liabilities will, therefore, apply in the case of an insolvent limited company.

The liquidator will declare a dividend as and when he is ready, but when he is in a position to do so he should send notice to the creditors.

There is no statutory form of notice required. A useful form is given on page 657.

(r) **Surplus after Payment of Liabilities.** After payment of the external liabilities if a surplus remains it belongs to the shareholders, and must be divided amongst them in accordance with their rights and interests.

The first step will be the repayment of capital. The holders of preference shares having a priority of capital are entitled to be repaid before the holders of other classes of shares, and if the latter are not fully paid this may involve the making of a further call on shares not fully paid in order to provide sufficient funds to pay out such preference shares.

If, however, the preference shares are not preferential as to capital the repayment must be made *pari passu* amongst all classes of shareholders.

ILLUSTRATION. The X Co., Ltd., in liquidation, after paying off all its external liabilities, had a cash surplus of £3,000.

REGISTER OF CREDITORS

Registered No.	Folio.	Name and Address.	Amount of Claim.			Amount Admitted.			Final Dividend @ 6/8 in £.			Remarks.
			£	s.	d.	£	s.	d.	£	s.	d.	
52	78	Capel & Jones, Broad Street Place, E.C.	1	16	5	1	16	5	1	12	2	
53	80	Cathling Valley Biscuit Co., Ltd., Cathling Valley	59	16	4	59	16	4	19	18	9	
54	83	Carter & Co., High Street N., Bromley ..	410	5	7	410	5	7	136	15	2	
55	80	Crude Iron Co., Dashwater Square, E. ..	567	0	3	310	10	0	103	10	0	
56	89	Cuthbert Jasper & Sons	16	15	10	—	—	—	—	—	—	
57	96	Daniel Picture Frame Co., Huddersfield	50	10	0	40	10	0	13	10	0	
58	99	Dennison & Dennison, Stratford, E. ..	1	16	11	1	16	11	12	4	4	
59	101	Denton & Payne, Huddersfield	100	1	0	90	16	4	30	5	5	
60	110	Dewcastle-on-Tyne Soap Works, Dewcastle-on-Tyne	1	10	0	—	—	—	—	—	—	
61	121	Dodds' Pin Box Co., Napier Works, Sudbury	17	19	5	17	18	6	5	19	6	
62	122	Fosstrevor & Stalheim, Ltd., Highgate ..	71	0	5	71	0	5	23	13	6	
63	124	Garvice, Ltd., Dublin	657	17	11	656	5	4	218	15	1	
64	125	W. Goodbine, Aldermanbury, E.C.	369	17	8	350	0	0	116	13	4	
65	126	Goodge & Rover, Willesden	10	6	6	10	6	6	3	3	6	
66	129	A. Grossmith & Co., 41 St. Stephen's Rd., Ealing	56	0	10	56	0	10	18	13	7	
67	135	M. A. Hales, Rue de las Paix, Paris ..	5	16	7	5	16	7	1	18	10	
68	139	J. H. Hobbs, Surrey Arms, Eltham ..	1	5	9	1	5	9	8	8	7	
69	145	J. Isaacs & Sons, Ludgate Circus, E.C. ..	78	15	0	78	15	0	26	5	0	
70	150	Jannersmith Electricity Works, Ltd., Jannersmith	369	0	0	369	0	0	123	0	0	
71	160	Jarvis & Payne, 79 Southminster Gate, W.	40	15	6	40	15	6	13	11	10	
72	164	A. B. Jenkins, 106 Langham Place, W.C.	100	6	11	90	1	0	30	0	4	
73	173	Jones & Broom, St. Saviour's Road, Hampstead	41	3	6	41	3	6	13	14	6	
74	180	Joynston Iron Works, Surbiton	36	5	7	36	5	7	12	1	10	

LONDON, E.C.2

1st July, 19..

X Y Z CO., LTD., IN LIQUIDATION

NOTICE OF DIVIDEND

NOTICE IS HEREBY GIVEN, that a first dividend of five shillings in the pound has been declared in this matter; and the same may be received at my office as above on Monday, the 6th day of July, 19.., or on any subsequent day between the hours of 10 a.m. and 4 p.m.

Amount of Admitted Proof -----

Amount of Dividend -----

(Sd.) A. B. C.,

Liquidator.

To -----

NOTE.—If it is desired that the remittance be sent by post, a written request to that effect, accompanied by the Receipt Form duly filled up and signed, must be lodged with me. Postal Remittances will be made at the risk of the payee only.

RECEIPT

Received of A. B. C., Liquidator of X Y Z Co., Ltd., in Liquidation, the sum of

Pounds shillings and pence, being the amount payable to $\frac{\text{me}}{\text{us}}$ in respect of

the first dividend of five shillings in the pound on $\frac{\text{my}}{\text{our}}$ claim against the Company.

Payee's Signature -----

has been conducted, and how the property of the company has been disposed of.

On the next page is a form of account suitable for presentation to the meeting.

Within one week of the meeting having been held the liquidator must make a return to the Registrar of Joint Stock Companies notifying the fact. The penalty for default in making this notification is £5 per day for every day during which the default continues.

At the expiration of three months from the date of the registration of such return the company is deemed to be dissolved, subject to all unclaimed moneys having been paid into the Companies Liquidation Account.

After the return of the final meeting has been given to the Registrar the Court may, on application, defer the date of dissolution; and after dissolution the Court may, on application declare the dissolution void at any time within two years.

(u) **Reconstructions.** A reconstruction may be defined as the selling of the undertaking of an existing company, to a new company specifically formed for that purpose. It may become necessary for any of the following causes—

(1) To effect an alteration in the domicile of the company.

(2) To alter the objects clause of the company's Memorandum otherwise than as permitted by Statute.

(3) For raising fresh capital by issuing partly paid shares in the new company in exchange for fully paid shares in the old company, and calling up the balance of such new shares as and when required. This becomes necessary when the old company cannot continue without acquiring fresh working capital, which it cannot otherwise obtain.

As regards the case of the issue of partly paid shares, this creates a liability on the part of the new shareholders. The original shareholders, however, cannot be compelled to take up these shares unless they wish to do so. Where there are dissentient shareholders, provided they give notice of dissent in time, they can either require the liquidator of the old company not to carry out the scheme, or to purchase their interest at a price which, if not settled by agreement, must be determined by arbitration.

Section 192 of the Companies (Consolidation) Act, 1908, under which reconstructions are usually carried out, runs as follows—

192.—“(1) Where a company is proposed to be, or is in course of being, wound up altogether voluntarily, and the whole or part of its business is proposed to be transferred or sold to another company (in this section called ‘the transferee company’), the liquidator of the first-mentioned company (in this section called ‘the transferor company’) may, with the sanction of a special resolution of that company, conferring

either a general authority on the liquidator, or an authority in respect of any particular arrangement, receive in compensation or part compensation for the transfer or sale, shares, policies, or other like interests in the transferee company, for distribution among the members of the transferor company, or may enter into any other arrangements whereby the members of the transferor company may, in lieu of receiving cash, shares, policies, or other like interests, or in addition thereto, participate in the profits of or receive any other benefit from the transferee company.

“(2) Any sale or arrangement in pursuance of this section shall be binding on the members of the transferor company.

“(3) If any member of the transferor company, who did not vote in favour of the special resolution at either of the meetings held for passing and confirming the same, expresses his dissent therefrom in writing addressed to the liquidator, and left at the registered office of the company within seven days after the confirmation of the resolution, he may require the liquidator either to abstain from carrying the resolution into effect, or to purchase his interest at a price to be determined by agreement, or by arbitration in manner provided by this section.

“(4) If the liquidator elects to purchase the member's interest, the purchase money must be paid before the company is dissolved, and be raised by the liquidator in such manner as may be determined by special resolution.

“(5) A special resolution shall not be invalid, for the purposes of this section, by reason that it is passed before or concurrently with a resolution for winding up the company, or for appointing liquidators; but if an order is made within a year for winding up the company, by or subject to the supervision of the Court, the special resolution shall not be valid unless sanctioned by the Court.

“(6) For the purposes of an arbitration under this section, the provisions of the Companies Clauses Consolidation Act, 1845, or, in the case of a winding up in Scotland, the Companies Clauses Consolidation (Scotland) Act, 1845, with respect to the settlement of disputes by arbitration, shall be incorporated with this Act, and in the construction of those provisions this Act shall be deemed to be the special Act, and ‘the company’ shall mean the transferor company; and any appointment by the said incorporated provisions directed to be made under the hand of the secretary, or any two of the directors, may be made under the hand of the liquidator, or if there is more than one liquidator, then of any two or more of the liquidators.”

THE X Y Z COMPANY. (In Liquidation.)

LIQUIDATOR'S STATEMENT OF ACCOUNT

FOR PRESENTATION AT THE

Final Meeting

TO BE HELD

SEPTEMBER 29TH, 19...

	£	s.	d.		£	s.	d.
To Cash in hand at commence-				By Liquidator's Expenses—			
ment of winding up	25	0	0	Costs	82	11	3
„ Realisation of Assets—							
Plant and Machinery ..	348	10	0	„ Liquidator's Remuneration	105	0	0
Stock	1,265	1	3	„ Preferential Creditors	184	0	0
Book Debts	1,471	3	5	„ Debenture Holders	£2,000		
Bills Receivable	100	0	0	Interest to date of			
				payment	50		
					2,050	0	0
				„ Unsecured Creditors—			
				First and Final Dividend			
				of 5s. 1d. in £ on £3,101	788	3	5
	£3,209	14	8		£3,209	14	8

It was at one time thought that where the sale of all the assets was authorised by the objects clause of the Memorandum of the selling company, a dissentient shareholder might be deprived of his right to claim to be bought out under Section 192 of the Companies (Consolidation) Act, 1908, and be forced to accept a new liability in respect of the shares received by way of purchase consideration of the old shares; and that if he did not accept such partly paid up shares he must necessarily lose his status as shareholder in the company, or accept whatever price for his shares the company might decide.

This contention was, however, negatived in the case of *Bisgood v. Henderson's Transvaal Estates, Ltd.* (1908, 1 Ch. 743). In this case the defendant company had power in its objects clause to sell all the assets of the company for shares, and entered into a scheme by which the new company was formed to take over its undertaking and assets, for a consideration consisting partly of the payment of its debts and liabilities, and partly in shares of the new company. Such shares were not fully paid up, however, and the scheme provided that the liquidator was to offer the shares in the new company, for distribution among the members of the old company. In the event of any of the members not accepting the shares, the liquidator was to sell the shares not accepted, and distribute the proceeds thereof among the non-accepting members, in proportion to the number of shares held by such persons in the old company. In the Chancery Division this was held to be a perfectly valid proceeding, but the Court of Appeal granted an injunction restraining the company from carrying out the reorganisation scheme.

In the course of his judgment Lord Justice Buckley, referring to the question of powers being taken in the objects clause of the Memorandum to sell the undertaking for shares, said—

"... The incorporation of a company is effected by the registration of a Memorandum of Association, which is to state the 'objects for which the proposed company is to be established.' To my mind that means the objects which the corporation during its corporate life is to pursue, the purpose by whose fulfilment it is to seek to earn profit. The definition of the objects is the definition of what is generally called the undertaking of the company. The modern practice is to add, but I think erroneously, an enumeration of powers for carrying these objects into effect. But, however that may be, the words 'the objects for which the proposed company is to be established' have, in my opinion, no relation to acts to be done after the corporate life has come to an end. So soon as the company passes into liquidation, the distribution of its assets is a matter which concerns the corporation not at all, but its creditors and

contributories only. In my judgment it is no part of the functions of the Memorandum of Association to define, under the corporate objects, the distribution of the assets after the corporate life is over. . . ."

"Distribution of capital (except on reduction of capital) can only be made in winding up. An agreement for sale may be a corporate act of the going company, and within its objects; but an agreement for sale and distribution can only be valid when the company 'is proposed to be wound up,' or is in course of being wound up. When the company is proposed to be wound up, or is in course of being wound up, Section 161 (now Section 192 of the Companies (Consolidation) Act, 1908), contains provisions which, in my judgment, define rights in the members, and which cannot by any clauses in the Memorandum and Articles of Association be excluded. If the company is proposed to be wound up, and the transaction is a sale and distribution, then in my opinion the Statute provides that sale by conversion into money may be replaced by exchange for shares, upon the terms, but only upon the terms of complying with the provisions of Section 161. It has been decided . . . that the rights of the members to dissent cannot be excluded by the Articles, but the argument before us is that the whole of the section may be excluded. I think not. . . ."

The effect of the judgment in this case is, that a company cannot sell the assets for partly paid shares in another company, and force its own shareholders to accept a *pro rata* distribution of such partly paid shares. If the selling company is authorised, and is in a position itself to hold the shares in the purchasing company, it could probably carry out such a scheme, since it need not then at once go into liquidation and distribute the shares amongst its members, but it must have funds to enable it to meet the calls upon such partly paid shares. But where the selling company is not in such a position, having no assets with which to discharge a future liability on the shares, it must distribute the shares amongst the members, and this can only be done in liquidation; so that immediately it is proposed to distribute the new shares among the members, the company must be considered as being proposed to be, or in course of being, wound up voluntarily. This being the case, a dissentient member may claim his remedies under Section 192.

There is nothing unjust or illegal in a scheme providing for the sale of the assets by a company so authorised for shares in another company, even if the scheme provides that—

- (a) the shares be partly paid;
- (b) the shares must be applied for within a limited time;
- (c) the shares not applied for shall be sold,

and the dissentient member shall take the proceeds;

since any such provisions will only apply where the dissentient fails to avail himself of the statutory remedy.

Fractions of shares in some cases require to be dealt with. One method is to allot the liquidator of the company concerned, the number of shares represented by the addition of the fractions. He will realise these shares at the best price possible and distribute the proceeds to the parties entitled thereto.

In other cases cash is paid in lieu of fractions of shares, while where the original shares which are being exchanged have a free market, fractional certificates are issued to the shareholders entitled thereto which have a marketable value. The fractional certificate entitles the holder on presentation of so many other certificates of a like value as will make up one share, to a certificate for one share; and the fractions are collected gradually in the market by the jobbers dealing in the stock who then in due course exchange them for complete certificates.

The Liquidation Account to the shareholders of the old company will show the share transactions as well as the receipts and payments of cash.

ILLUSTRATION.—The books of the Asiatic Patents Company, Ltd., contained the following balances—

	£	s.	d.	£	s.	d.
Share Capital: 15,000						
Shares of £1 each,						
paid				15,000	0	0
Sundry Creditors . .				14,000	0	0
Plant and Machinery . .	4,000	0	0			
Stock	2,000	0	0			
Patent Rights	15,000	0	0			
Sundry Debtors	6,000	0	0			
Preliminary Expenses . .	500	0	0			
Profit and Loss A/c . .	1,475	0	0			
Cash	25	0	0			
	£29,000	0	0	29,000	0	0

The company being unable to raise further capital and the patents standing in the books at a figure largely in excess of their value, it was found necessary to reconstruct the company and the following scheme was submitted to the shareholders and creditors—

(1) The company to go into voluntary liquidation and a new company with a nominal capital of £30,000 to be called the Eastern Patents Company, Ltd., to take over the assets and liabilities.

(2) The liabilities were to be discharged by the new company on the following basis—

	£	s.	d.
Preferential to be paid in full	150	0	0
To receive 10s. in £ in full settlement	6,000	0	0
„ receive par value in 6% Debentures, fully paid	7,850	0	0
	£14,000	0	0

(3) 15,000 shares of £1 each, 10s. per share paid, to be issued to the shareholders of the old company, the balance of 10s. per share being payable on allotment.

(4) The costs of liquidation to be paid by the new company, as part of the purchase consideration. These amounted to £201 15s. 0d.

All the unsecured creditors agreed to the proposals, but five shareholders holding 1,000 shares dissented and required their interests to be purchased. The price of 7s. 6d. per share was agreed upon, which was paid to the liquidator by one of the assenting shareholders in return for the allotment of such shares. Show the liquidator's final account. (See next page.)

(v) **Disposal of the Books.** In the case of a voluntary liquidation the liquidator should, at the final meeting get an extraordinary resolution as to the disposal of the books of the company, and if he gets this he can dispose of the books in such manner as may be authorised thereby.

It is presumed, however, that a liquidator should not destroy or otherwise dispose of the books for a period of at least two years after the company is dissolved, since under Section 223 of the Companies (Consolidation) Act, 1908, the Court may on the application of an interested person make an order declaring dissolution to have been void at any time within two years of the date of dissolution.

Section 222 of the Companies (Consolidation) Act, 1908, provides that after five years from the dissolution of the company, no responsibility shall rest on the company or the liquidator, or any person to whom the custody of the books and papers has been committed, by reason of the same not being forthcoming to any person claiming to be interested therein.

(w) **Special Powers of the Liquidator.** In the following matters the powers of a liquidator are greater than those of the directors of a company which is a going concern—

(1) He can compromise calls. The directors of a company cannot do this since it would amount to the issue of shares at a discount.

(2) He can sell all the assets without power in the objects clause and distribute the proceeds amongst the parties entitled thereto.

(3) He can call up a reserve liability of capital.

(4) He can set aside a fraudulent preference.

It must be remembered, also, that although the functions of the directors cease upon the company going into liquidation they may be continued by the company in general meeting, or revived by the liquidator for any special purpose, e.g. for forfeiture of shares.

(x) **Powers of the Liquidator as against Receiver.** Where all the assets are charged to debenture holders and a Receiver is appointed, if the company goes into liquidation a liquidator is still

ASIATIC PATENTS COMPANY, LTD. (In Liquidation.)

LIQUIDATORS' ACCOUNT OF RECEIPTS AND PAYMENTS

FOR PRESENTATION TO THE FINAL MEETING TO BE HELD 29TH SEPTEMBER, 19..

RECEIPTS.				PAYMENTS.										
		Cash.		Shares.	Debentures.				Cash.		Shares.	Debentures.		
	£	s.	d.		£	s.	d.		£	s.	d.	£	s.	d.
Received from Eastern Patents Co., Ltd.—								By Costs of Liquidation—						
15,000 Shares of £1 each :								Liquidator's Remn. ..	105	0	0			
10s. paid in Eastern Patents Co., Ltd.								Costs and Expenses ..	96	15	0			
								.. Creditors—						
				15,000				.. Preferential .. £ 150	150	0	0			
£7,850 6% Debentures of Eastern Patents Co., Ltd.								.. Compounded at 10% in £	6,000	0	0			
								.. Received Deben- .. tures at par ..	3,000	0	0			
									7,850			7,850	0	0
									<u>14,000</u>					
Cash	3,351	15	0					.. Shareholders—						
								.. Paid to dissentients ..	375	0	0			
Received from A. B. for purchase of Dissentients' Shares	375	0	0					£1 Shares : 10s. paid in Eastern Patents, Ltd.—						
								Dissentients' Shares taken up by A. B. ..				1,000		
								Distribution to Assenting Shareholders, being 1 new share for each original share				14,000		
	£ 3,726	15	0	15,000	7,850	0	0		£ 3,726	15	0	15,000	7,850	0
	£													

required. In such a case the duty of the liquidator is as follows—

- (1) To make proper statutory returns.
- (2) To see that preferential creditors are paid where debentures are secured by a floating charge.
- (3) To examine Receiver's accounts with a view to challenging any payments improperly made.
- (4) He is entitled to the custody of the books but must produce them to the Receiver where necessary.
- (5) To make calls. If the uncalled capital is charged in favour of the debenture holders the Court will only allow the call to be made in the winding up, and it will be the duty of the liquidator to make the call; and unless the Court authorises the Receiver to get the call in, the liquidator will have to take the necessary steps for obtaining the money from the contributories, and should arrange with the Receiver for his remuneration in respect of this.

(6) The liquidator must also receive the equity (if any), *i.e.* take over the surplus assets after the debenture holders have been satisfied in full.

It will be evident from the foregoing that the offices are somewhat incompatible since the Receiver will be entirely concerned with the interests of the debenture holders, whereas the liquidator must be concerned with the interest of all the parties.

In the case of a company which is already being wound up by the Court, however, the Court will usually appoint the Official Receiver as receiver for the debenture holders.

COMPROMISES.—In any liquidation the liquidator is not enabled to make a compromise on his own responsibility. Under Section 214 of the Companies (Consolidation) Act, 1908, the liquidator may—

"(a) Pay any classes of creditors in full;

"(b) Make any compromise or arrangement with creditors or persons who claim to be creditors, or having or alleging themselves to have any claim, present or future, certain or contingent, ascertained or sounding only in damages against the company, or whereby the company may be rendered liable.

"(c) Compromise all calls or liability to calls, debts and liabilities capable of resulting in debts and all claims present or future, certain or contingent, ascertained or sounding only in damages, subsisting or supposed to subsist between the company or contributory or alleged contributory or other debtor or person apprehending liability to the company, and all calls in any way relating to or affecting the assets of the winding up of the company on such terms as may be agreed and take any security for the discharge of any such call, debt, liability or claim, and give a complete discharge in respect thereof."

The authority required to enable him to make

any of these compromises is, in voluntary liquidation, an extraordinary resolution of the company; in a supervision liquidation, the sanction of the Court; and in a compulsory liquidation the sanction of the Court or the Committee of Inspection.

Any compromise entered into under Section 214 by the liquidator is subject to the control of the Court and any creditor or contributory may apply to the Court in respect of any exercise or proposed exercise of the powers conferred by this section.

It will, of course, be understood that in all these cases the sanction is merely an authority to the liquidator, and no creditor or contributory will be bound unless he himself assents to the proposal.

Under Section 191 of the Act it is provided that in voluntary liquidation any arrangement entered into between a company about to be or in the course of being wound up voluntarily and its creditors, shall be binding on the company if sanctioned by an extraordinary resolution, and on the creditors if acceded to by three-fourths in number and value of the creditors.

Any creditor or contributory may, within three weeks of the completion of such an arrangement, appeal to the Court against it and the Court may thereupon as it thinks just, amend, vary, or confirm the arrangement.

In view of the fact that any such arrangement under Section 191 is liable to be upset on appeal, the section is seldom used, and where it is desired to enter into an arrangement with creditors, Section 120, which applies to all classes of liquidations and also to arrangements with creditors and contributories, is more often adopted.

Under this section it is provided that where a compromise or arrangement is proposed between a company and its creditors, or any class of them, or between a company and its members or any class of them, the Court may, on application of the company or of any creditor or member of the company or of the liquidator, order a meeting of the creditors or class of creditors, or of the members of the company or class of members as the case may be, to be summoned in such manner as the Court directs.

If a majority in number representing three-fourths in value of the creditors or class of creditors, or members or class of members, as the case may be, present either in person or by proxy at the meeting, agree to any compromise or arrangement, the compromise or arrangement shall, if sanctioned by the Court, be binding on the creditors or class of creditors, or members or class of members as the case may be, and also on the liquidator and contributories of the company.

The procedure under Section 120 is most desirable where a compromise with a class is required, since if properly passed and sanctioned it will be binding on all parties and will not be liable to be upset. It is desirable that in any accounts

required the fact of a compromise having been given effect to should be clearly stated.

SUPERVISION LIQUIDATION.—(a) **Voluntary Liquidation.** An order for winding up under the supervision of the Court can only be made where the company concerned is already in voluntary liquidation.

The principal advantage arising from such an order is that the Court, on making it, at once stays all actions and distrains, and may give general directions as to the conduct of the liquidation. This prevents the necessity for continual applications to the Court in respect of such matters.

The liquidator is appointed by the Court, having regard to the wishes of the creditors or contributories as provided by sufficient evidence. Unless the Court otherwise orders, the voluntary liquidator remains in office, but the Court may appoint another to act with him.

(b) **Powers of the Liquidator.** The powers of the liquidator are the same as if the company were wound up altogether voluntarily, subject only to the variation of those powers contained in the order for supervision. The usual directions in the order are that the liquidator shall, in each quarter, file with the Registrar a report in writing as to the position of, and the progress made with, the winding up, and that no costs or remuneration of the liquidator or any other person are to be paid out of the assets of the company unless taxed or allowed by the Registrar.

The Court may also impose further restrictions (e.g. that the list of contributories shall be settled by the Court), or that the liquidator shall act under the directions of a Committee of Inspection.

To enable the liquidator to compromise under Section 214, leave of the Court is necessary.

Under Section 120, the procedure is the same as in voluntary liquidation.

The liquidator cannot sell the assets for shares in another company without leave of Court.

The commencement of the liquidation being the voluntary liquidation preceding it, preferential payments must be calculated up to that date and not to the date of the petition or order.

(c) **The Accounts.** The accounts to be kept in a supervision liquidation will be similar to those in voluntary liquidation. There are no special forms of accounts, nor are the accounts subjected to any audit.

The Court may, however, in the order, direct the accounts to be passed in chambers, in which case they will have to be prepared and vouched in the same manner as the accounts of a receiver.

WINDING UP UNDER THE ORDER OF THE COURT.—(a) **Essential Differences between Voluntary and Compulsory Liquidations.** In voluntary liquidation, the liquidator is primarily appointed by the company as agent of and

trustee for the company, and carries out the liquidation on his own responsibility.

He has to obtain sanction for making compromises or arrangements, or to sell the assets of the company for shares in another company. He has also to make the statutory returns under Section 224, and is thereby controlled to a limited extent by the Board of Trade; and he may be controlled by the Court under Section 193 of the Companies (Consolidation) Act, 1908; but, apart from these matters, he has a free hand in conducting the liquidation.

In compulsory liquidation, however, the liquidator is appointed by, and is an officer of, the Court, and is also trustee for the creditors. He is under the control of the Board of Trade in all questions of administration, and he is required to account to the Board of Trade; and strict regulations are laid down by both the Act and the Winding-up Rules as to the whole of his conduct in the management of the liquidation.

(b) **Appointment and Remuneration.** The appointment of the liquidator is made by the Court on the nomination of separate meetings of creditors and contributories. The Court will generally appoint the person nominated if both meetings decide on the same person; but, if they differ, the Court must decide the difference, and in such a case will generally prefer the decision of that body which has the chief interest in the realisation of the assets.

The remuneration of the liquidator is fixed by the Committee of Inspection, unless the Court otherwise orders, and must be in the nature of a commission or percentage, of which one part shall be payable on the amount realised after deducting the sums (if any) paid to secured creditors other than debenture holders, out of the proceeds of their securities, and the other part on the amount distributed in dividend. If there is no Committee of Inspection, it is in accordance with the scale of percentage payable for realisations and distributions by the Official Receiver as liquidator.

If the Board of Trade is of opinion that the remuneration of a liquidator as fixed by the Committee of Inspection is unnecessarily large, the Board of Trade may apply to the Court, and thereupon the Court shall fix the remuneration of the liquidator.

The liquidator is required to give security to the satisfaction of the Board of Trade, but the cost of this cannot, as in bankruptcy, be charged against the estate; the liquidator must bear the charge personally.

(c) **Statement of Affairs.** It is clearly no part of the duty of the liquidator to prepare the Statement of Affairs, but it is desirable to show in relation to the accounts the manner in which this statement is made up.

A Statement of Affairs in the prescribed form

must be verified by affidavit and submitted in duplicate to the Official Receiver, who files a verified copy within fourteen days of the winding-up order.

The persons responsible for the making up of the statement are those who are directors at the time of the winding up, and the secretary or other chief officer of the company; or such persons having been officers of the company within one year of the order or having taken part in the formation of the company, as the Official Receiver (subject to the directions of the Court) may require to submit and verify the same.

The statement must show—

(1) The particulars of the assets, debts, and liabilities of the company;

(2) The names, residences, and occupations of the creditors and contributories of the company;

(3) The securities held by creditors, with the dates when the securities were given;

(4) A Deficiency Account, showing how the company's income has been expended.

(5) Such further or other information as may be prescribed, or as the Official Receiver may require.

On the following pages is the official form of the Statement of Affairs.

In connection with the preparation of the statement, it must be noted that expenses incurred in connection therewith cannot be allowed out of the assets of the company, unless the Official Receiver's sanction is obtained. In order to obtain this, a statement of the estimated cost must be submitted to the Official Receiver; and, if the sanction is duly given, the costs can be paid in their specified order.

(d) **Books and Accounts.** The Companies Winding-up Rules require the following books and accounts to be kept, viz.—

Record Book;

Cash Book;

Trading Account.

(1) **RECORD BOOK.** The Official Receiver, until a liquidator is appointed, and thereafter the liquidator, must keep a Record Book in which to enter all the minutes of proceedings had and resolutions passed at any meeting of creditors or contributories, or at any meeting of the Committee of Inspection, and all such matters as may be necessary to give a correct view of the administration of the company's affairs.

The liquidator is not bound to insert therein any document of a confidential nature, such as the opinion of counsel, on any matter affecting the interests of the creditors or contributories, nor need he exhibit such document to any person other than a member of the Committee of Inspection.

The Record Book must show the authority for

all acts which require sanction, such as the making of a compromise, employment of a solicitor, etc.; but the mere entry in this book of any such authority will not justify any illegal proceedings.

(2) **CASH BOOK.** The liquidator must keep a Cash Book in the form directed by the Board of Trade, and enter therein from day to day the receipts and payments made by him. The form prescribed is given on page 669.

(3) **TRADING ACCOUNT.** Where a business is carried on with the sanction of the Court or the Committee of Inspection, a distinct account of the trading must also be kept, and the total weekly accounts of receipts and payments on such Trading Account must be incorporated in the Cash Book.

The form of Trading Account is shown on page 670.

INSPECTION OF BOOKS. Any creditor or contributory may, subject to the control of the Court, personally or by his agent inspect the books.

ACCOUNTING BY THE OFFICIAL RECEIVER. Where a liquidator other than the Official Receiver is appointed, the Official Receiver must account to him. If the liquidator is dissatisfied with the account or any part thereof, he may report the matter to the Board of Trade, which will take such action as it may deem expedient.

(e) **Dealing with Moneys.** The liquidator must pay all moneys received by him into the Companies Liquidation Account kept by the Board of Trade at the Bank of England in such a manner and at such times as the Board of Trade directs, and he is entitled to a certificate therefor.

He must not pay any sums received by him as liquidator into his private banking account, but is entitled to open a special account for the purpose of clearing moneys prior to remitting the same to the official account.

Remittances should be made to the Companies Liquidation Account weekly, sums of £200 or more being paid in forthwith. If the liquidator retains more than £50 (or such amount as the Board of Trade may in any particular case authorise him to retain) for more than ten days, he is liable to pay interest on the amount retained in excess, at 20 per cent. per annum, to have his remuneration disallowed in whole or in part, to be removed from office by the Board of Trade, and to pay any expenses occasioned by his default.

As moneys are received or paid the entries relating thereto should be made in the Cash Book, the same being continually kept up to date.

Moneys received in respect of the trading will be entered in the Trading Account and the total of the receipts and payments will be entered in the General Cash Book weekly.

The use of a local bank instead of the Companies Liquidation Account may be authorised by the Board of Trade if the committee satisfies the

No. C. 26.

Statement of Affairs

In the

Court of

IN THE MATTER OF THE COMPANIES (CONSOLIDATION) ACT, 1908, AND
IN THE MATTER OF *THE GENERAL TRADING COMPANY, LIMITED.
STATEMENT OF AFFAIRS on the 31st December, 19.., the date of the Winding-up Order.
(1) AS REGARDS CREDITORS.

* Insert full
Name of
Company.

Gross Liabilities.	LIABILITIES.	Expected to rank.	ASSETS.	Estimated to Produce.
£ s. d.	£ s. d.	£ s. d.	£ s. d.	£ s. d.
10,386 0 0	Debts and Liabilities, viz.— (a) (State number) Unsecured Creditors as per List "A"	10,386 0 0	(a) Property as per List "H," viz.— (a) Cash at Bankers (b) " " in hand (c) Stock-in-trade (Estimated cost, £15,000) (d) Machinery (e) Trade fixtures, fittings, utensils, etc. (f) Investments in shares, etc. (g) Loans on Mortgage (h) Other property, viz.—	3 0 0 11,000 0 0
8,090 0 0	(b) Creditors fully secured (not including debenture holders) as per List "B"	8,090 0 0	(b) Book debts (Good Doubtful Bad Estimated to produce	9,265 0 0 980 0 0
4,510 0 0	(c) Creditors partly secured as per List "C"	4,510 0 0	(c) Bills of Exchange or other similar securities on hand, as per List "J"	320 0 0
420 0 0	Less estimated value of securities	3,120 0 0	(d) Surplus from securities in the hands of creditors fully secured (per contra) (b)	100 0 0
140 0 0	Estimated to rank for dividend	1,400 0 0	(e) Unpaid calls (Debtors as per List "K" : Estimated to produce Estimated total assets Deduct preferential creditors as per contra (f)	21,668 0 0 140 0 0 21,528 0 0 10,300 0 0
10,300 0 0	(d) Liabilities on Bills discounted other than the Company's own acceptances for value, as per List "D"	1,400 0 0	Estimated amount available to meet claims of debenture holders Deduct loans on debenture bonds secured on the assets of the Company as per contra (g)	11,228 0 0 968 0 0 £12,196 0 0
	(e) Other liabilities as per List "E"	140 0 0	Estimated amount available to meet unsecured creditors, subject to cost of liquidation	
	(f) Preferential Creditors for rates, taxes, wages, etc., as per List "F" deducted contra		Estimated deficiency of assets to meet liabilities of the Company, subject to cost of liquidation	
	(g) Loans on debenture bonds as per List "G"	10,300 0 0		
	() Deducted contra and interest (holders).			
	Estimated surplus (if any) after meeting liabilities of Company, subject to cost of liquidation			
£33,846 0 0		£12,196 0 0		

The nominal amount of unpaid capital liable to be called up is £50, which is [available to meet above deficiency] or [charged to debenture holders], or as the case may be.

Dr.

(II.) AS REGARDS CONTRIBUTORIES

Cr.

	£	s.	d.	£	s.	d.		£	s.	d.
Capital issued and allotted, viz.—							Estimated Surplus as above (if any) subject			
100 Founders' Shares of £1 per Share (Shareholders).							to cost of Liquidation			
(a) Issued as fully paid.										
Amount called up at 10s. per Share, as per List "L"		50	0	0						
15,000 Ordinary Shares of £1 per Share (Shareholders)	15,000	0	0							
(a) Issued as fully paid.										
Amount called up at £ . . . per Share, as per List "M"										
5,000 Preference Shares of £1 per Share (Shareholders).										
(a) Issued as fully paid.										
Amount called up at £1 per Share, as per List "N"	5,000	0	0							
(b)										
Amount (if any) paid in advance of calls										
	£20,050	0	0							
Less unpaid calls estimated to be irrecoverable	50	0	0							
Add deficiency to meet liabilities as above				20,000	0	0	Total deficiency as explained in Statement "O"	20,968	0	0
				968	0	0				
				£20,968	0	0		£20,968	0	0

(a) Where capital is issued as partly paid up, the form should be altered accordingly.

(b) Add particulars of any other capital.

No. C. 32.

Statement of Affairs.

List "O" (1).

LIST "O" (1), DEFICIENCY ACCOUNT

(1) Deficiency Account where Winding-up Order made WITHIN THREE YEARS OF formation of Company

	£	s.	d.		£	s.	d.
I. Gross profit (if any) arising from carrying on business from date of formation of Company to date of Winding-up Order				I. Expenses of carrying on business from date of formation of Company to date of Winding-up Order, viz.—			
II. Deficiency as per Statement of Affairs				Salaries and Wages	£	s.	d.
				Rent, Rates, and Taxes			
				Miscellaneous Trade Expenses			
				Depreciation written off in Company's Books			
				Interest on Loans			
				II. Bad Debts (if any) as per List "I" (1)			
				III. Directors' Fees from date of formation of Company to date of Winding-up Order			
				IV. Dividends paid (if any) from date of formation of Company to date of Winding-up Order			
				V. Losses on investments realised from date of formation of Company to date of Winding-up Order (exclusive of depreciation written off as above), viz. (4)			
				VI. Depreciation of Property not written off in Company's Books, viz. (4)			
				VII. Other Losses and Expenses (if any) (2) from date of formation of Company to date of Winding-up Order, viz. (4)			
Total amount to be accounted for . . . (3) £				Total amount accounted for (3) £			

NOTES.—(1) This list must show when debts were contracted.

(2) Here add particulars of other losses or expenses (if any) and liabilities (if any) for which no consideration received.

(3) These figures should agree.

(4) Where particulars are numerous, they should be inserted in a separate Schedule.

Signature _____

Dated _____ 19__

CASH BOOK

RECEIPTS.

PAYMENTS.

Date.	PARTICULARS.
	Total.
	Drawn from Bank.
	Debits Collected.
	Property Realised.
	Receipts from Securities held by Creditors.
	Calls.
	Other Receipts.
	Date.
	PARTICULARS.
	Voucher Nos. (in red).
	Total.
	Paid into Bank.
	Board of Trade and Court Fees.
	Law Costs of Petition.
	Law Costs after Winding-up Order.
	Remuneration of Man- ager and Liquidator.
	Official Receiver's Com- mission on Assets Rea- lised, and Amount Dis- tributed in Dividend or Paid to Contributories.
	Charges of Auctioneer, Accountant, Shortland Writer, etc., as taxed.
	Notices in <i>Gazette</i> and Local Paper.
	Incidental Expenses, in- cluding Possession.
	Preferential Creditors and Rent.
	Payments to redeem Securities.
	Dividends Paid.
	Repayment to Contributories.
	Other Payments.

No. 88. (Rule 171.)

LIQUIDATOR'S TRADING ACCOUNT UNDER SECTION 155

(Title.)

G. H. the liquidator of the above-named Company in account with the estate

RECEIPTS.					PAYMENTS.				
Dr.					Cr.				
Date.					Date.				

Liquidator.

(Date)

We have examined this account with the vouchers and find the same correct, and we are of opinion the expenditure has been proper.

Dated this day of 19

Committee of Inspection
[or Member of the Committee of Inspection].

Board that for the purpose of carrying on the business of the company, obtaining advances, or for any other reason it is for the advantage of the creditors or contributories that an account should be opened with a bank other than the Bank of England.

The Board of Trade authorises the liquidator to keep such account at such bank as the committee may select for such time and on such terms as the committee may think fit, and the liquidator must forthwith pay all moneys received by him into that account to the credit of the liquidator of the company.

All payments on the local bank account are made by cheque payable to order, and every cheque must have marked or written on the face of it the name of the company, and must be signed by the liquidator and countersigned by at least one member of the Committee of Inspection and such other person (if any) as the Committee of Inspection may appoint. No stamps are required on the cheques.

If the Board of Trade is of opinion that the local bank is no longer required for the purposes mentioned in the application therefor, it may at any time order the account to be closed.

The following is the form of application for a local bank account prescribed by the Companies Winding-up Rules, 1909—

No. 82. (Rule 165.)

APPLICATION TO BOARD OF TRADE
TO AUTHORISE A SPECIAL BANK ACCOUNT

(Title.)

We, the Committee of Inspection, being of opinion that Mr. of , the liquidator in the above matter, should have a special bank account for the purpose of (a) hereby apply to the Board of Trade to authorise him to make his payments into and out of the bank.

All cheques to be countersigned by , a member of the committee of inspection, and by for

Dated this day of

..... } Committee of
..... } Inspection.

a Here insert grounds of application.

(f) Settling the List of Contributories. In order to determine the persons from whom moneys

are due in respect of share capital not paid up, a list of contributories must be prepared and settled by the liquidator as an officer of the Court. The list contains a statement of the address and the number of shares or extent of interest to be attributed to each contributory; and distinguishes between the several classes of contributories, *i.e.* persons who are contributories in their own right, and persons who are contributories as being liable for the debts of others. Heirs and devisees should not be placed on the list in addition to the legal personal representative, but may be added as and when the liquidator thinks fit.

The prescribed form has already been given in the part dealing with Voluntary Liquidation.

The liquidator gives notice in writing of the time and place appointed for the settlement of the list to every person he proposes to include in the list, stating in what character and for what number of shares or interest he is to be included.

He hears any person objecting to be settled on the list, and finally settles the list, which, when so settled, is the list of contributories of the company; and forthwith gives notice to every person finally placed on the list; which notice must state in what character and for what number of shares or interest he has been placed on the list; and must inform such person that any application for the removal of his name from the list, or for a variation of the list, must be made to the Court by summons within twenty-one days of the date of service of the notice. The Court may extend the time or allow an application to be made although it has expired.

By a direction of the Court only members whose shares are not fully paid up, and who are therefore liable to contribute to the assets of the company, need be taken into account in settling the list of contributories.

The liquidator may from time to time vary or add to the list, but any variation or addition must be made in the same way as the settlement of the original list.

In Compulsory Liquidation, as in Voluntary Liquidation, there are two lists, the A List and the B List, and the same principles apply as have already been mentioned in connection therewith.

The following are the official forms under the Companies Winding-up Rules, 1909, relating to the settlement of the List.

No. 42. (Rule 77.)

PROVISIONAL LIST OF CONTRIBUTORIES TO BE MADE OUT BY LIQUIDATOR.

(Title.)

The following is a list of members of the company liable to be placed on the list of contributories of the

said company, made out by me from the books and papers of the said company, together with their respective addresses and the number of shares [or extent of interest] to be attributed to each so far as I have been able to make out or ascertain the same.

In the first part of the list, the persons who are contributories in their own right are distinguished.

In the second part of the said list, the persons who are contributories as being representatives of, or being liable to the debts of others, are distinguished.

FIRST PART.—CONTRIBUTORIES IN THEIR OWN RIGHT

Serial No.	Name.	Address.	Description.	Number of Shares [or extent of Interest].

SECOND PART.—CONTRIBUTORIES AS BEING REPRESENTATIVES OF, OR LIABLE TO THE DEBTS OF, OTHERS

Serial No.	Name.	Address.	Description.	In what Character included.	Number of Shares [or extent of Interest].

No. 43. (Rule 78.)

NOTICE TO CONTRIBUTORIES OF APPOINTMENT TO SETTLE LIST OF CONTRIBUTORIES

(Title.)

Take Notice that I, _____ the liquidator of the above-named company, have appointed the _____ day of _____ 19____, at _____ of the clock in the _____ noon, at (a) _____, in the county of _____, to settle the list of the contributories of the above-named company, made out by me, pursuant to the Companies (Consolidation) Act, 1908, and the rules thereunder, and that you are

* Insert place of appointment.

In the matter of
SECOND PART.—CONTRIBUTORIES AS BEING
REPRESENTATIVES OF OR LIABLE TO THE
DEBTS OF OTHERS

Limited.
of the Registrar at (a) and on any day between
the hours of and
Dated this day of 19 .
(Signed)
Liquidator.

Serial No. in List.	Name.	Address.	Description.	In what Character included.	Number of Shares [or extent of Interest.]	Date when included in the List.

To Mr.
[or to Mr.
his solicitor].
(a) State address.

No. in List.	Name.	Address.	Description.	In what Character included.	Number of Shares [or extent of Interest].

In the matter of
The SECOND SCHEDULE above referred to.

Limited.

Serial No. in List.	Name.	Address.	Description.	In what Character proposed to be included.	Number of Shares [or ex- tent of Interest.]	Date when excluded from the List.

No. 47. (Rule 82.)
SUPPLEMENTAL LIST OF CONTRIBUTORIES
(Title.)
1. The following is a list of persons who, since making out the list of contributories herein, dated the day of 19 , I have ascertained are, or have been, holders of shares in [or members of] the above-named company, and to the best of my judgment are contributories of the said company.
2. The said supplemental list contains the names of such persons together with their respective addresses and the number of shares [or extent of interest] to be attributed to each.
3. In the first part of the said list such of the said persons as are contributories in their own right are distinguished.
4. In the second part of the said list such of the said persons as are contributories as being representatives of, or being liable to the debts of others, are distinguished.
[The supplemental list is to be made out in the same form as the original list.]

No. 46. (Rule 80.)
NOTICE TO CONTRIBUTORY OF FINAL SETTLEMENT
OF LIST OF CONTRIBUTORIES AND THAT HIS
NAME IS INCLUDED
(Title.)

Take notice that I, , the liquidator of the above-named company, have, by certificate, dated the day of 19 , under my hand, finally settled the list of contributories of the said company, and that you are included in such list in the character and for the number of shares [or extent of interest] stated below.

Any application by you to vary the said list of contributories, or that your name may be excluded therefrom, must be made by you to the Court within 21 days from the service on you of this notice, or the same will not be entertained.

The said list may be inspected by you at the chambers

No. 48
AFFIDAVIT OF SERVICE OF NOTICE TO
CONTRIBUTORY
(Title.)
I, (a) of , make
oath and say as follows—
1. I did on the day of 19 ,
in the manner hereinafter mentioned, serve a true copy
of the notice now produced and shown to me and
(a) State full description of the deponent.

marked "A," upon each of the respective persons whose names, addresses, and descriptions appear in the second, third, and fourth columns of the First Schedule to the list of contributories of the said Company made out by the [Official Receiver and] Liquidator of the Company on the day of 19 , and now on the file of proceedings of the said Company, except that in the tabular form at the foot of such copies respectively I inserted the number on list, name, address, description in what character included, and (b) of the person on whom such copy of the said notice was served in the same words and figures as the same particulars are set forth in the said schedule.

2. I served the said respective copies of the said notice, by putting such copies respectively, duly addressed to such persons respectively, according to their respective names and addresses appearing in the said schedule, by placing the same prepaid in the Post Office at before the hour of o'clock in the noon of the said day of 19 .
Sworn, etc.

(b) "Number of shares" or "extent of interest."

No. 49. (Rule 81.)

ORDER ON APPLICATION TO VARY LIST OF CONTRIBUTORIES

(Title.)

Upon the application of *W.N.*, by summons dated the day of 19 , for an order that the list of contributories of the company and the liquidator's certificate finally settling the same be varied by excluding the name of the applicant therefrom [*or, as the case may be*], and upon hearing, etc., and upon reading, etc., It is Ordered, That the list of contributories of the company and the liquidator's certificate finally settling the same be varied by excluding the name of the said *W.N.* from the said list of contributories, *or* by including the name of the said *W.N.* as a contributory in the said list for shares, [*or, as the case may be*] [*or* the Court does not think fit to make any order on the said application, except that the said *W.N.* do pay to the liquidator of the said company his costs of this application, to be taxed in case the parties differ].

(g) **Realisation of Assets.** The liquidator must take all the necessary steps for the purpose of realising the assets of the company to the best advantage. What has been said with regard to this matter in the portion of this article dealing with Voluntary Liquidation will apply equally in Compulsory Liquidation.

It must be remembered, however, that if it is desired to sell the assets for shares in another company, sanction of the Court must be obtained before this is done.

The liquidator may take out in his official name letters of administration to any deceased contributor, and do in his official name any other act which may be necessary for obtaining

payment of any money due from a contributory or his estate, and which cannot conveniently be done in the name of the company.

He may also prove, claim, rank and draw a dividend in the bankruptcy of a contributory.

The getting in of uncalled capital is also a very important matter, and any steps taken for this purpose must be carried out strictly in accordance with the Rules made, which are as follows: When the liquidator desires to make a call he may summon a meeting of the Committee of Inspection for the purpose of obtaining its sanction to the intended call.

The notice must be sent to each member of the Committee so as to reach him not less than seven days before the time appointed for the meeting; and must contain a statement of the proposed amount of the call and the purpose for which it is intended.

Notice is also advertised once in a daily newspaper, and, when the winding up is not in the High Court, in a newspaper circulating in the district of the Court in which the winding up is taking place.

The advertisement states the time and place of the meeting of the Committee; so that each contributory may attend and be heard, or make any communication in writing to the liquidator or members of the Committee to be laid before the meeting in reference to the intended call. These statements or representations to the liquidator or the Committee must be considered before the call is sanctioned.

The sanction of the Committee is given by resolution, passed by a majority of the members present.

When there is no Committee, the liquidator cannot make a call without the leave of the Court.

Leave of the Court may be obtained by summons stating the amount of the call, served four clear days before the day appointed for making the call on every contributory proposed to be included; but the Court may direct service by advertisement without separate notice to each contributory.

When a call has been made a copy of the resolution or order is served upon every contributory included in such call, together with a notice from the liquidator specifying the amount of balance due; the resolution or order need not be advertised unless for any special reason the Court so directs. A copy of the document making the call is to be filed with the Registrar.

Payment of a call is enforced by order of the Court, called a Balance Order, made in Chambers on summons by the liquidator.

The following are the official forms under the Companies Winding-up Rules, 1909, relating to calls—

No. 50. (Rule 83 (1).)

NOTICE TO EACH MEMBER OF COMMITTEE
OF INSPECTION
OF MEETING FOR SANCTION TO PROPOSED CALL

(Title.)

Take notice that a meeting of the Committee of Inspection of the above company will be held at
on the (a) day of 19 ,
at o'clock in the noon, for the purpose
of considering and obtaining the sanction of the
committee to a call of £ per share proposed
to be made by the liquidator on the contributories.

Annexed hereto is a statement showing the necessity
for the proposed call and the amount required.

Dated this day of 19 .

(Signed)

Liquidator.

(a) To be a date not less than seven days from the date when the
notice will in course of post reach the person to whom it is addressed.

STATEMENT.

1. The amount due in respect of proofs admitted against the company,
and the estimated amount of the costs, charges, and expenses
of the winding up, form in the aggregate the sum of £ or thereabouts.

2. The assets of the company are estimated to realise the sum of £.
There are no other assets, except the amounts due from
certain of the contributories to the company, and in my opinion it
will not be possible to realise in respect of the said amounts more
than £.

3. The list of contributories has been duly settled, and persons have
been settled on the list in respect of the total number of shares.

4. For the purpose of satisfying the several debts and liabilities of
the company, and of paying the costs, charges, and expenses of the
winding up, I estimate that a sum of £ will be required in
addition to the amount of the company's assets hereinbefore mentioned.

5. In order to provide the said sum of £ it is necessary
to make a call on the contributories, and having regard to the probability
that some of them will partly or wholly fail to pay the amount of the
call, I estimate that for the purpose of realising the amount required,
it is necessary that a call of £ per share should be made.

(Annex tabular statement showing amounts of debts, costs, etc., and
of assets.)

No. 51. (Rule 83 (2).)

ADVERTISEMENT OF
MEETING OF COMMITTEE OF INSPECTION
TO SANCTION PROPOSED CALL

(Title.)

Notice is hereby given that the undersigned liquidator
of the above-named company proposes that a
call should be made "on all the contributories of the
said company," or, as the case may be,
of £ per share, and that he has summoned a
meeting of the Committee of Inspection of the company
to be held at
on the day of 19 , at
o'clock in the noon, to obtain their sanction to
the proposed call.

Each contributory may attend the meeting, and be
heard or make any communication in writing to the
liquidator or the members of the Committee of
Inspection in reference to the intended call.

A statement showing the necessity of the proposed
call and the purpose for which it is intended may be

obtained on application to the liquidator at his office
at (a).

Dated this day of 19 .
Liquidator.

(a) Insert address.

No. 52. (Rule 83 (4).)

RESOLUTION OF COMMITTEE OF INSPECTION
SANCTIONING CALL

Resolved, that a call of £ per share be
made by the liquidator on all the contributories of the
company [or, as the case may be].

(Signed)

Members of the Committee
of Inspection.

Dated this day of 19 .

No. 53. (Rule 86.)

NOTICE OF CALL
SANCTIONED BY COMMITTEE OF INSPECTION
TO BE SENT TO CONTRIBUTORY

(Title.)

Take notice that the Committee of Inspection in the
winding up of this company have sanctioned a call of
per share on all the contributories of
the company.

The amount due from you in respect of the call is
the sum of £ . This sum should be paid by
you direct to me at my office (a) on or
before the day of 19 .

Dated this day of 19 .

To Mr.

Liquidator.

(a) State address.

No. 54. (Rule 84.)

SUMMONS FOR LEAVE TO MAKE A CALL

(Title.)

Let the several persons whose names and addresses
are set forth in the second column of the schedule
hereto, being contributories of the above-named company,
as shown in the third column of the said schedule,
attend at on the day
of 19 , at o'clock in the
noon, on the hearing of an application on the part
of the [Official Receiver and] liquidator of the company
for an order that he may be at liberty to make
a call to the amount of per share on all the
contributories [or as the case may be] of the said
company.

Dated the day of 19 .

This summons was taken out by of
Solicitors for the [Official Receiver
and] liquidator.

To

NOTE.—If you do not attend either in person or by
your Solicitor, at the time and place above-mentioned,
such order will be made and proceedings taken as the
Court may think just and expedient.

SCHEDULE

Number on List.	Name and Address.	In what character included.

No. 55. (Rule 84.)

AFFIDAVIT OF LIQUIDATOR
IN SUPPORT OF PROPOSAL FOR CALL

(Title.)

I, _____ of, etc., the liquidator of the above-named company, make oath and say as follows—

1. I have in the schedule now produced and shown to me, and marked with the letter A, set forth a statement showing the amount due in respect of the debts proved and admitted against the said company, and the estimated amount of the costs, charges, and expenses of and incidental to the winding up the affairs thereof, and which several amounts form in the aggregate the sum of £ _____ or thereabouts.

2. I have also in the said schedule set forth a statement of the assets in hand belonging to the said company, amounting to the sum of £ _____ and no more. There are no other assets belonging to the said company, except the amounts due from certain of the contributories of the said company, and, to the best of my information and belief, it will be impossible to realise in respect of the said amounts more than the sum of £ _____ or thereabouts.

3. _____ persons have been settled by me on the list of contributories of the said company in respect of the total number of _____ shares.

4. For the purpose of satisfying the several debts and liabilities of the said company and of paying the costs, charges, and expenses of and incidental to the winding up the affairs thereof, I believe the sum of £ _____ will be required in addition to the amount of the assets of the said company mentioned in the said Schedule A, and the said sum of £ _____.

5. In order to provide the said sum of £ _____, it is necessary to make a call upon the several persons who have been settled on the list of contributories as before mentioned; and, having regard to the probability that some of such contributories will partly or wholly fail to pay the amount of such call, I believe that, for the purpose of realising the amount required as before-mentioned, it is necessary that a call of £ _____ per share should be made.

Sworn, etc.

No. 56. (Rule 84.)

ADVERTISEMENT OF INTENDED CALL

In the matter of _____
Notice is hereby given that the (a) _____ Court
has appointed _____ the _____ day
of _____ 19 _____, at _____ o'clock in the _____ noon,
at (b) _____, to sanction a call on all the
contributories of the said company [or as the case may
be] and that the liquidator of the said company pro-
poses that such call shall be for £ _____ per
share. All persons interested are entitled to attend
at such day, hour, and place, to offer objections to
such call.

Dated this _____ day of _____ 19 _____.

Liquidator.

(a) Name of Court.

(b) State place of appointment.

No. 57. (Rule 84.)

ORDER GIVING LEAVE TO MAKE A CALL

The _____ day of _____ 19 _____.

(Title.)

Upon the application of the [Official Receiver and] liquidator of the above-named company, and upon reading the affidavit of the said [Official Receiver and] liquidator, filed the _____ day of _____ 19 _____, and the exhibit marked "A" therein referred to, and an affidavit of

filed the _____ day of _____ 19 _____.

It is ordered that leave be given to the [Official Receiver and] liquidator to make a call of £ _____ per share on all the contributories of the said company. (a)

And it is ordered that each such contributory do on or before the _____ day of _____ 19 _____, pay to the [Official Receiver and] liquidator of the _____ company, the amount which will be due from him or her in respect of such call.

(a) Or as the case may be.

No. 58. (Rule 85.)

DOCUMENT MAKING A CALL

(Title.)

I, _____ the [Official Receiver and] Liquidator
of the above-named company, in pursuance of (a) _____
made (or passed) this _____ day
of _____ 19 _____, hereby make a call of
per share on all the contributories of the company,
which sum is to be paid at my office (b) _____
on the _____ day of _____ 19 _____.

Dated this _____ day of _____ 19 _____.

(a) An order of Court, or resolution of the Committee of Inspection.

(b) Insert address.

No. 59. (Rule 86.)

NOTICE TO BE SERVED
WITH THE ORDER SANCTIONING A CALL
(Title.)

The amount due from you, *A. B.*, in respect of the call made pursuant to leave given by the above [*or within*] order is the sum of £ , which sum is to be paid by you to me as the liquidator of the said company at my office, No. Street,

Dated this day of 19 .
To Mr. *A. B.*

Liquidator.

No. 60. (Rule 87.)

AFFIDAVIT IN SUPPORT OF APPLICATION FOR ORDER
FOR PAYMENT OF CALL
(Title.)

I, of, etc., the liquidator of the above-named company, make oath and say as follows—

1. None of the contributories of the said company, whose names are set forth in the schedule hereto annexed, marked "A," have paid or caused to be paid the sums set opposite their respective names in the said schedule, which sums are the amounts now due from them respectively under the call of

per share, duly made under the Companies (Consolidation) Act, 1908, dated the day of 19 .

2. The respective amounts or sums set opposite the names of such contributories respectively in such schedule are the true amounts due and owing by such contributories respectively in respect of the said call.

"A."

THE SCHEDULE ABOVE REFERRED TO

No. on List.	Name.	Address.	Description.	In what Character included.	Amount due.
					£ s. d.

Sworn, etc.

NOTE.—In addition to the above affidavit, an affidavit of the service of the application for the call will be required in cases in which the Committee of Inspection or the Court has authorised a call to be made.

No. 61. (Rule 87.)

ORDER FOR PAYMENT OF CALL DUE FROM
A CONTRIBUTORY

The day of 19 .
(Title.)

Upon the application of the liquidator of the above-named company, and upon reading an affidavit of

filed the day of 19 ,
and an affidavit of the liquidator, filed the day of 19 , it is ordered that *C. D.*, of, etc. [*or E. F.*, of, etc., the legal personal representative of *L. M.*, late of, etc., deceased], one of the contributories of the said company [*or, if against several contributories*, the several persons named in the second column of the schedule to this order, being respectively contributories of the said company], do, on or before the day of 19 , or within four days after service of this order, pay to the liquidator of the said company at his office, No. Street, in the county of , the sum of £ , [*if against a legal personal representative add*, out of the assets of the said *L. M.*, deceased, in his hands as such legal personal representative as aforesaid, to be administered in due course of administration, if the said *E. F.* has in his hands so much to be administered, *or, if against several contributories*, the several sums of money set opposite to the respective names in the sixth column of the said schedule hereto], such sum [*or sums*] being the amount [*or amounts*] due from the said *C. D.* [*or L. M.*], [*or the said several persons respectively*], in respect of the call of £ per share duly made, dated the day of 19 .

THE SCHEDULE
REFERRED TO IN THE FOREGOING ORDER

No. on List.	Name.	Address.	Description.	In what Character included.	Amount due.
					£ s. d.

Note.—The copy for service of the above order must be endorsed as follows—

"If you, the undermentioned *A. B.*, neglect to obey this order by the time mentioned therein, you will be liable to process of execution, for the purpose of compelling you to obey the same."

No. 62. (Rule 87.)

AFFIDAVIT OF SERVICE OF ORDER
FOR PAYMENT OF CALL

(Title.)

I, *J. B.*, of, etc., make oath and say as follows—

1. I did on the day of 19 , personally serve *G. F.*, of , in the county of , etc., with an order made in this matter by this Court, dated the day of 19 , whereby it was ordered [*set out the order*] by delivering to and leaving with, the said *G. F.*, at , in the county of , a true copy of the said order, and at the same time producing and showing unto him the said *G. F.*, the said original order.

2. There was endorsed on the said copy when so served the following words, that is to say, "If you,

the undermentioned G. F., neglect to obey this order by the time mentioned therein, you will be liable for process of execution for the purpose of compelling you to obey the same."

Sworn, etc.

A debenture holder who is also indebted to the company cannot, if the debentures give a charge on the book debts, receive any benefit from the debentures, either by way of principal or interest, till he has paid all that is due to the company.

A company in liquidation which holds shares in another company, also in liquidation, cannot claim to set off debts against calls. As between contributories and the company, there can be no set off of a debt against calls, unless the contributory is bankrupt, in which case his trustee in bankruptcy may set off against calls any debt due to the bankrupt from the company otherwise than as a member of the company.

The following is the form of proof—

No. 63. (Rules 88-93.)

PROOF OF DEBT. GENERAL FORM.

(Title.)

I (a) _____ of _____ in the county of _____, make oath and say:

(a) Fill in full name, address, and occupation of deponent. If proof made by creditor, strike out clauses (b) and (c). If made by clerk of creditor, strike out (c). If by clerk or agent of the company, strike out (b).
(d) Insert "me and to C. D. and E. F., my co-partners in trade (if any)," or, if by clerk or agent, insert name, address, and description of principal.
You should attend carefully to these directions.

(b) That I am in the employ of the undermentioned creditor, and that I am duly authorised by _____ to make this affidavit, and that it is within my own knowledge that the debt hereinafter deposed to was incurred and for the consideration stated, and that such debt, to the best of my knowledge and belief, still remains unpaid and unsatisfied.

(c) That I am duly authorised, under the seal of the company hereinafter named to make the proof of debt on its behalf.

1. That the above-named company was, at the date of the order for winding up the same, viz., the _____ day of _____ 19____, and still is justly and truly indebted to (d) _____ in the sum of _____ pounds _____ shillings and _____ pence for (e) _____ as shown by the account endorsed hereon, or by the following account, viz.—

for which sum or any part thereof I say that I have not nor hath (f) _____ order to my knowledge or belief for (g) _____ use had or received any manner of satisfaction or security whatsoever, save and except the following (h)—

: :
Admitted to vote for
£ : : day
the _____ of 19____
NOTE THIS.
Official Receiver
or Liquidator.

(e) State consideration [as goods sold and delivered by me (and my said partner) to the company between the dates of] [or moneys advanced by me in respect of the undermentioned bill of exchange] [or, as the case may be].
(f) My said "partners or any of them" or "the above-named creditor" [as the case may be].
(g) "My," or "our," or "their," or "his" (as the case may be).
(h) [Here state the particulars of all securities held, and where the securities are on the property of the company assess the value of the same, and if any bills or other negotiable securities be held specify them in the schedule.]
Admitted to rank for dividend for
£ : : day
this _____ of 19____
Official Receiver
or Liquidator.

Sworn at _____ this _____ day of _____
Before me

Date.	Drawer.	Acceptor.	Amount.	Due date.

NOTE.—The proof cannot be admitted for voting at the first meeting unless it is properly completed and lodged with the Official Receiver before the time named in the notice convening the meeting.

(h) **Proofs.** A proof is an affidavit verifying a debt. It must be made by the creditor, or by some person duly authorised by him, and must state the debt, the date on, and the consideration for, which it was incurred, and particulars of any security held. If the amount of the debt exceeds £2, the proof must be stamped with a shilling proof stamp.

If the Official Receiver continues to act as liquidator, he need not finally admit or reject proofs until he gives notice of his intention to declare a dividend.

A liquidator other than the Official Receiver, however, must take over all proofs from the Official Receiver, giving him a receipt for them. He must examine such proofs, and if not already dealt with by the Official Receiver, he must admit or reject them within twenty-eight days of receiving them, and must similarly deal with any proofs sent in to him personally.

If a proof is rejected, written notice of rejection must be given to the creditor. If it is admitted, the notice of dividend is sufficient notice of admission. The creditor may appeal to the Court against the rejection within twenty-one days of receiving notice thereof.

If appeal against rejection is notified, the liquidator, within three days of receiving such notice, must file the rejected proof with the registrar of the Court, with a memorandum thereon of his disallowance.

Where the Official Receiver is acting, he must, before payment of a dividend, file all proofs tendered in the winding up, with a list thereof, distinguishing in such list the proofs which were wholly or partly admitted and the proofs which were wholly or partly rejected.

A liquidator, other than the Official Receiver, must, on the first day of every month, file with the registrar a certified list of all proofs received by him during the month next preceding, distinguishing therein the proofs admitted, those rejected, and those that stand over for further consideration; and in the case of proofs admitted or rejected, he must cause the proofs to be filed with the registrar.

If the liquidator thinks that a proof has been improperly admitted, he may, after notice to the creditor, apply to the Court to expunge the proof or reduce its amount. If the amount of the debt exceeds £200, the application must be held in open Court. If the liquidator declines to interfere, a creditor may apply.

The liquidator may administer affidavits for the purpose of proof: such proof may be made by the creditor himself or by some person authorised on his behalf, and, if made by the person so authorised, it must state his authority and means of knowledge; and in any case, this affidavit must specify the vouchers by which the claim is

substantiated, for which vouchers the liquidator may call at any time.

All trade discounts must be deducted, and so also must any cash discount in excess of 5 per cent.

Where there are numerous claims for wages by workmen and others employed by the company, one proof for all such claims may be made, either by a foreman or by some other person, on behalf of all such creditors. The proof must have annexed to it, as forming part thereof, a schedule, setting forth the names of the workmen and others and the amounts severally due to them. In such a case, no stamp is required.

A debt not due at the date of the winding-up order may be proved for, subject to a rebate of interest at 5 per cent. from the date of declaration of dividend till the due date.

Rent and other periodical payments are apportionable, and a proportionate part may be proved for up to the date of the winding-up order.

Where there are mutual debts, mutual credits, or mutual dealings between the company and a creditor, the two accounts are to be set off against each other, and only the resulting balance is to be paid or proved for.

Mutual debts are debts of the same degree, both due at once; mutual credits, where the debts are of different degrees, or where one is due immediately and the other at a future time; and mutual dealings are transactions which will result in debts.

The account for set-off is to be taken at the date of the presentation of petition.

The following is the form of Proof of Debt of Workmen—

No. 64. (Rule 99.)
PROOF OF DEBT OF WORKMEN
(Title.)

I (a)
(b)

of

make an oath and say:

1. That the above-named company was on the day of , 19 , and still is justly and truly indebted to the several persons whose names, addresses, and descriptions appear in the schedule endorsed hereon in sums severally set against their names in the sixth column of such schedule for wages due to them respectively as workmen or others in the employ of the company in respect of services rendered by them respectively to the company during such periods as are set out against their respective names in the fifth column of such schedule, for which said sums, or any part thereof, I say that they have not, nor hath any of them had or received any manner of satisfaction or security whatsoever.

Sworn at
in the county of
this day of
19 .

Before me

} Deponent's Signature.

(a) Fill in full name, address, and occupation of deponent.

(b) On behalf of the workmen and others employed by the above-named company.

SCHEDULE referred to on the other side.

1. No.	2. Full Name of Workman.	3. Address.	4. Description.	5. Period over which Wages due.	6. Amount due.
					£ s. d.

Signature of Deponent

The following are the official forms under the Companies' Winding-up Rules, 1909, relating to Proofs, apart from those already given and those dealt with (*infra*) under the heading of *Dividends*—

No. 65. (Rule 103.)

NOTICE OF REJECTION OF PROOF OF DEBT

(Title.)

Take notice, that, as [Official Receiver and] Liquidator of the above-named company, I have this day rejected your claim against the company (a) [to the extent of £] on the following grounds :

And further take notice, that, subject to the power of the Court to extend the time, no application to reverse or vary my decision in rejecting your proof will be entertained after the expiration of (b) days from this date.

Dated this day of 19 .

Signature

Address

To [Official Receiver and] Liquidator.

(a) If proof wholly rejected, strike out words underlined.

(b) Twenty-one days or seven days, as the case may be.

No. 66. (Rule 110.)

LIST OF PROOFS

TO BE FILED UNDER RULES 110 AND 111

(Title.)

I hereby certify that the following is a correct list of all proofs tendered to me in the above matter during the past month.

Dated this day of 19 .
Liquidator.

Name of Creditor	Proofs Tendered.					
	Amount of Proof.			Whether admitted, rejected, or standing over for further consideration.	If admitted, Amount.	
	£	s.	d.		£	s. d.

(i) **Payments.** The assets must be applied in payment of the debts, costs, etc., in proper order. Secured creditors must first be paid out of their securities, and after this the costs of the liquidation. Preferential creditors are next in priority, and after this the unsecured creditors. If there is any surplus, it will be returnable to contributors in accordance with their rights and interests.

(1) **SECURED CREDITORS.** A secured creditor, that is, one holding a mortgage, charge or lien on some property of the debtor, has three courses open to him. He may—

(1) Rely on his security and not prove at all ;

(2) Surrender his security and prove for the full amount of the debt ;

(3) Realise or estimate his security, deduct the realised or estimated amount from his debt, and prove for the balance both for voting and dividend.

When a secured creditor estimates his security for voting purposes, the liquidator may, within twenty-eight days of its being so used for voting, claim to take the security at the estimated value plus 20 per cent. ; but the creditor may, at any time before he accepts the offer of the liquidator, re-estimate, and the liquidator may then take it at the new estimation.

After this twenty-eight days, if the estimate be used for purposes of dividend, the liquidator may claim to take the security at the estimated value, or to have it put up for auction, when both the liquidator and the creditor may bid. The creditor may at any time amend the valuation and proof, upon showing to the satisfaction of the liquidator or the Court that the valuation and proof were made *bonâ fide* on a mistaken estimate, or that the security has diminished or increased in value since its previous valuation. But every such amendment must be made at the cost of the creditor, and upon such terms as the Court shall order, unless the liquidator allows the amendment without application to the Court. Actual notice by the liquidator to redeem at the estimated value does not prevent this right of revaluation from being exercised.

A secured creditor who has estimated the value of his security may, in writing, call upon the liquidator to state whether he intends to take it at the estimated value, or to have it put up for auction ; and if within six months the liquidator fails to claim it, or makes no reply, the creditor may convert the security to his own use, and still prove for the balance of his debt. If the liquidator elect to take the security at the creditor's valuation after this notice, no re-estimate can be made by the creditor.

It must be remembered that where debentures are secured by a fixed or floating charge on the

assets of the company, the holders of such debentures will be secured creditors.

(2) COSTS. After payment of the fees and actual expenses incurred in realising or getting in the assets, the costs are payable in the following order :

(i) The taxed costs of the petition, including the taxed costs of any person appearing on the petition whose costs are allowed by the Court ;

(ii) The remuneration of the special manager (if any) ;

(iii) The costs and expenses of any person who makes, or concurs in making, the company's Statement of Affairs ;

(iv) The taxed charges of any shorthand writer appointed to take an examination ; provided that, where the shorthand writer is appointed at the instance of the Official Receiver, the cost of the shorthand notes shall be deemed to be an expense incurred by the Official Receiver in getting in and realising the assets of the company ;

(v) The liquidator's necessary disbursements, other than actual expenses of realisation otherwise provided for ;

(vi) The costs of any person properly employed by the liquidator with the sanction of the Committee of Inspection ;

(vii) The remuneration of the liquidator ;

(viii) The actual out-of-pocket expenses necessarily incurred by the Committee of Inspection, subject to the approval of the Board of Trade.

(3) PREFERENTIAL CREDITORS. Preferential creditors rank in priority to the ordinary unsecured creditors, and if there are insufficient assets to pay them in full, they must abate *pari passu*.

For full particulars as to the preferential creditors, reference should be made to the Section relating thereto in *Voluntary Liquidation* (p. 653).

It must be remembered that preferential creditors rank for payment in priority to the holders of debentures secured by a floating charge, although the latter are entitled to be recouped as far as may be necessary out of any assets of the company available for the payment of general creditors.

The preference is calculated up to the date of the winding-up order.

(4) UNSECURED CREDITORS. The unsecured creditors rank next for payment, taking *pari passu* in respect of admitted proofs.

The holder of a bill of exchange, of which the company is acceptor, is entitled to prove and draw dividends in respect of the bill ; but he is not a secured creditor, and must, therefore, rank amongst the unsecured creditors.

The holder of a bill of exchange which has been endorsed by the company can also prove for the amount of the bill, but in this case the company is only contingently liable ; and if the bill is duly

met by the acceptor, nothing can be claimed from the estate of the company.

Where proof is made in respect of a bill of exchange, the instrument must be produced and marked by the Official Receiver or liquidator ; and upon payment of dividend it must again be exhibited, so that the amount of dividend paid can be endorsed thereon.

The procedure when the liquidator desires to declare a dividend is as follows—

Not more than two months before declaring a dividend, the liquidator must give notice of his intention to do so to—

(a) The Board of Trade (who gazette same) ;

(b) Such of the creditors mentioned in the Statement of Affairs as have not proved their debts.

The notice must specify the latest date up to which proofs may be lodged, which must not be less than fourteen days from the date of such notice. This time may be extended by the Court.

Proofs sent in response to this notice must be admitted or rejected within fourteen days from the latest date fixed for sending in proofs.

Notice of appeal from rejection of proof, after such last-mentioned date, must be given within seven days from the date of the notice of the decision against which the appeal is made ; and in such case the liquidator must make provision for the dividend upon such proof and the probable costs of the appeal in the event of the proof being admitted.

The time for such appeal may be enlarged by the Court. Immediately after the time fixed for such appeal has expired, the liquidator proceeds to declare a dividend, and gives notice to the Board of Trade (who gazette same).

Dividends may, at the request and risk of the creditors, be sent to them by post.

A creditor who has not proved his debt before the declaration of a dividend, is entitled to be paid such dividend out of any money for the time being in the hands of the liquidator. Such a creditor will receive this unpaid dividend before payment of future dividends, but he cannot upset any dividend already declared before his debt was proved.

Before declaring a final dividend, the liquidator must give notice in the manner prescribed to persons who have notified their claims to him, but have not established them to his satisfaction, that if they do not establish their claims to the satisfaction of the Court within the time limited by the notice, he will proceed to make a final dividend without regard to their claims.

Upon declaration of a dividend, a list of proofs filed with the Registrar must be sent to the Board of Trade. If the winding up is in a County Court, the list must be examined by the Registrar with

the actual proofs and, if found correct, certified by him.

If the winding up is in the High Court, office copies of all lists of proofs filed by the liquidator must be transmitted to the Board of Trade, if required by them. The payment of dividends will, except where a local bank has been authorised, be made by cheques on the Bank of England, or money orders will be prepared by the Board of Trade on the application of the liquidator, and will be transmitted to him for distribution among the creditors. The application for these cheques and orders must be made in the prescribed form; and must be certified by the Registrar if the proceedings are in a County Court and by the liquidator if the proceedings are in the High Court, in the latter case being accompanied by office copies of the list of proofs filed.

Ten days' notice is required by the Board of Trade to enable cheques and money orders to be prepared; and each item on the list sent in should be numbered consecutively, so that corresponding numbers may be affixed on the cheques or orders.

If the dividend is paid through a local bank, the cheques will be prepared by the liquidator; but a certified list of proofs or an office copy of the list of proofs filed if the proceedings are in the High Court, must be sent in, and vouchers for dividends paid must be forwarded for audit.

(5) INTEREST. In cases where a debt bears interest, either by contract or at law, proof can be made for the debt and interest up to the date of the winding-up order or receiving order, as the case may be, under the following circumstances—

(i) Judgments, money paid by a surety, and moneys due under an award.

(ii) If the debt be due on a written instrument which is overdue.

(iii) If written notice has been given of the intention to charge interest after a certain date.

In the above cases, 4 per cent. is allowed; but bills of exchange overdue carry interest at 5 per cent.

If a definite rate of interest has been agreed upon, that amount can be proved for, up to the date of the winding-up order, for voting purposes; but not more than 5 per cent. can rank for dividend till all creditors are paid in full.

Interest can, however, be proved for after the date of the winding-up order, in the case of a debt which is due at a future time by virtue of a written instrument which bears interest on the face of it. In such cases, two proofs must be made: first, for the original debt, with interest at the stipulated rate not exceeding 5 per cent. up to the date of the order. If a dividend should be declared before the due date, a rebate of 5 per cent. must be made from the amount of the dividend from the date of declaration to the due

date. A second proof must be made for interest at the stipulated rate not exceeding 5 per cent. from the date of the order till the due date; no rebate need be made on the dividend on this proof.

The limitations as to the amount of stipulated interest which can be received only apply where proof is made for the amount; and do not, therefore, apply on the realisation of securities. A secured creditor who has stipulated for interest at a rate exceeding 5 per cent. can, on realising the security, retain the debt with stipulated interest up to the date of payment, if the proceeds are sufficient.

The following are the official forms under the Companies Winding-up Rules, 1909, relating to dividends—

No. 67. (Rule 150.)

NOTICE TO CREDITORS OF INTENTION TO DECLARE DIVIDEND

(Title.)

A (a) dividend is intended to be declared in the above matter. You are mentioned in the Statement of Affairs, but you have not yet proved your debt.

If you do not prove your debt by the _____ day of _____ 19____, you will be excluded from this dividend.

Dated this _____ day of _____ 19____.

Liquidator,
[Address.]

To X. Y.

(a) Insert here "first" or "second," or "final," or as the case may be.

No. 68. (Rule 150 (5).)

CERTIFIED LIST OF PROOFS UNDER RULE 150 (5) COMPANIES (WINDING UP) RULES, AND APPLICATION FOR ISSUE OF CHEQUES FOR DIVIDEND ON COMPANIES LIQUIDATION ACCOUNT.

Companies Liquidation Account.
Ledger Folio _____.

Re _____ Court _____ No. _____ 1 _____.

I hereby certify that the following list has been compared with the proofs filed, and that the names of the creditors and the amounts for which the proofs are admitted are correctly stated.

(Signature) *

Dated the _____ day of _____ 19____.

I certify that by my books the sum of £ _____ stands to the credit of the above Company with the Companies Liquidation Account at the Bank of England, and that the sum of £ _____ is required to meet the undermentioned dividends, on proofs which have been duly made and admitted to rank for dividend upon the Company, and I have to request that orders for payment may be issued to me.

The dividend is payable on the _____ day of _____ 19____, and notice of declaration

* If the proceedings are in a County Court, to be signed by the Registrar. If the proceedings are in the High Court, to be signed by the Liquidator.

AUTHORITY FOR DELIVERY

SIR,

PLEASE deliver to

(Insert the name of the person who is to receive the cheque or money order, or the words " $\frac{me}{us}$ by post,"at " $\frac{my}{our}$ risk," if you wish it sent to you in that way.)the cheque or money order for the dividend payable to $\frac{me}{us}$ in this matter.

Payee's signature.

To the [Official Receiver and] Liquidator.

No. 72. (Rule 150 (7).)

AUTHORITY TO LIQUIDATOR
TO PAY DIVIDENDS TO ANOTHER PERSON

(Title.)

To the [Official Receiver and] Liquidator.

SIR,

$\frac{I}{We}$ hereby authorise and request you to pay to M of (a specimen of whose signature is given below), all dividends as they are declared in the above-named matter, and which may become due and payable to $\frac{me}{us}$ in respect of the proof of debt for the sum of £ , against the above-named Company, made [by Mr.] on $\frac{my}{our}$ behalf.

And $\frac{I}{we}$ further request that the cheque or cheques drawn in respect of such dividends may be made payable to the order of the said M whose receipt shall be sufficient authority to you for the issue of such cheque or cheques in his name.

It is understood that this authority is to remain in force until revoked by $\frac{me}{us}$ in writing.

Signatures

Witness to the Signature
ofWitness to the Signature
of

Date

Specimen of Signature of person appointed
as above.Witness to the Signature
ofWitness to the Signature of person appointed
as above.

(6) CONTRIBUTORIES. After all the liabilities have been met, any surplus will be returned to contributories. The same principles will apply as

have already been set out under the heading relating thereto in *Voluntary Liquidation* (p. 644).

The list showing the amount due to each contributory is entered on the prescribed form and filed with the Registrar, together with an affidavit by the liquidator to the effect that the claims of creditors have been fully satisfied, and that a surplus of £ is available for distribution amongst the shareholders.

A summons is then issued by the liquidator to adjust the rights of the creditors *inter se*, to pay persons named in the affidavit the sums entered against their names in the "net return payable" column.

The liquidator may not without special leave of the Court rectify the Register of Members; but a shareholder may assign his interest in the form of an ordinary transfer, and upon making a return to the contributories, it will be the duty of the liquidator to bring such transfer to the notice of the Court, and the Court will have regard to the claims of the assignee.

The following are the official forms under the Companies Winding-up Rules, 1909, relating to Returns to Contributories—

No. 73. (Rule 151.)

NOTICE OF RETURN TO CONTRIBUTORIES

Cheques are cancelled at the expiration of six months from date of issue, and money orders at the expiration of twelve months from month of issue.

A fee of 1s. when the return does not exceed £1, and 2s. 6d. when the return exceeds £1, is chargeable on the re-issue, after cancellation, of cheques and money orders—the fee being payable in Companies (Winding Up) Stamps.

[Please bring this Notice with you.]

(Title.)

Return of £ per share.

[Address]

[Date]

Notice is hereby given that a return of per share has been declared in this matter, and that the same may be received at my office, as above, on the day of 19 , or on any subsequent day, except Saturday, between the hours of .

Upon applying for payment, this notice must be produced entire, together with the share certificate. If you do not attend personally, you must forward the share certificate and fill up and sign the subjoined Forms of *Receipt* and *Authority*, when a cheque or money order payable to your order will be delivered in accordance with the *Authority*.

(Signed)

Liquidator.

NOTE.—The receipt should be signed by the contributory personally, or in the case of joint contributories by each.

RECEIPT

No. 19 .

Received of the sum of pounds in this matter the
and pence, being the amount payable
to in respect of the return
of per share held by in this
company.

Contributory's signature

£ : :

AUTHORITY FOR DELIVERY

SIR,

PLEASE deliver to

(Insert the name of the person who is to receive the
cheque or money order, or the word: " $\frac{me}{us}$ by post," at
" $\frac{my}{our}$ risk," if you wish it sent to you in that way.)

the cheque or money order for the return payable to
 $\frac{me}{us}$ in this matter.

Contributory's signature

To the [Official Receiver and] Liquidator.

(j) **The Audit of Accounts.** The Cash Book must be audited by the Committee of Inspection not less than once every three months and the day on which it was audited must be certified by them.

The Trading Account must from time to time, not less than once in every month, be verified by affidavit and submitted to the Committee of Inspection (if any) or such member thereof as may be appointed by the committee for that purpose, who must examine and certify the same.

At the expiration of six months from the winding up order and at the expiration of every six months till the release of the liquidator, or when the assets have been fully realised and distributed (even though six months have not elapsed) duplicate copies of the Cash Book for the period must be sent to the Board of Trade together with the necessary vouchers and copies of the certificates of audit by the Committee of Inspection ; also a report in such form as the Board of Trade directs.

The documents which it is necessary to send to the Board of Trade are the following—

(1) A complete copy of the Estate Cash Book with analysis columns, which is retained by the Board of Trade, and an affidavit verifying the same.

No. 74. (Rule 151.)

SCHEDULE OR LIST OF CONTRIBUTORIES HOLDING PAID-UP SHARES TO WHOM A DIVIDEND
OR RETURN IS TO BE PAID

In the matter of				No.		of 19				
Number in settled List.	Name of Contribu- tory as in settled List.	Address.	Number of Shares held as per settled List.	Total called-up Value.	Total paid-up Value.	Arrears of Calls at date of Return.	Previous returns of capital appropri- ated by Liquidator for Arrears of Calls.	Amount of Return payable at..... per share.	Net Return payable.	Date and particulars of transfer of interest or other variation in List.

(2) A copy of the Estate Cash Book containing bank and total columns only.

(3) The Trading Accounts, together with vouchers and affidavits verifying the same.

(4) Special Manager's Account (if any) with vouchers and affidavit.

(5) Receipts for all cash payments, with allocators where the same are subject to taxation.

(6) Vouchers relating to assets realised, e.g., marked catalogue of auctioneer and account rendered by him.

(7) The Record Book.

(8) Bank Pass Book where local bank has been authorised, together with certificate of bank balance.

(9) Order on the Companies Liquidation Account authorising the payment of the Board of Trade audit fees.

(10) Lists of dividends, distinguishing between those paid and those unclaimed relating to creditors and contributories respectively.

(11) Report as to the position of the estate in the prescribed form.

With the first accounts sent to the Board of Trade for audit, a summary of the Statement of Affairs must be forwarded, showing thereon in red ink the amounts realised and giving explanations of the cause of non-realisation of such assets as are not yet realised.

On the occasion of every audit the liquidator must also transmit to the Board of Trade with his accounts a summary in the prescribed form which, after approval by the Board of Trade, must be printed, and forward the necessary number of copies to the Board of Trade, duly stamped for posting to the creditors and contributories.

Allocators (*i.e.* Taxing Master's Certificate) must be forwarded for all charges taxable, and the amount of costs paid in respect of each special matter should be separately stated as far as possible.

If part of the assets be sold through an auctioneer or other agent, the gross proceeds of the sale must be paid over by the auctioneer or agent, and his charges afterwards paid on production of the taxing master's certificate. The liquidator who employs him is accountable for the proceeds of the sale, unless the Court otherwise orders. The Board of Trade will not pass the accounts unless the gross proceeds are brought to credit.

The audit fees charged by the Board of Trade are as follows: After deducting money spent in carrying on the business of the company and amounts paid by the Official Receiver or liquidator to secured creditors (other than debenture holders)

On the first £	5,000 realised (gross) or fraction thereof	1	per cent.
" next £	9,500	"	" $\frac{1}{2}$ "
" "	£400,000	"	" $\frac{1}{4}$ "
" "	£500,000	"	" $\frac{1}{2}$ "
Above £1,000,000	"	"	" 1/16 "

The Board of Trade certifies that the account has been duly passed and a duplicate copy also certified is filed with the Court. Each copy is open to the inspection of any creditor or other interested person.

Where a liquidator has neither received nor paid any sum of money since the last audit he must forward to the Board of Trade an affidavit of no receipts or payments.

The following is the form of certificate by Committee of Inspection as to audit of liquidator's accounts prescribed by the Companies Winding-up Rules, 1909—

No. 86. (Rule 169.)

CERTIFICATE BY COMMITTEE OF INSPECTION
AS TO AUDIT OF LIQUIDATOR'S ACCOUNTS

(Title.)

We, the undersigned, members of the Committee of Inspection in the winding up of the above-named company, hereby certify that we have examined the foregoing account with the vouchers, and that to the best of our knowledge and belief the said account contains a full, true, and complete account of the liquidator's receipts and payments.

Dated this day of , 19 .

} Committee of Inspection.

The Certificate relating to the Trading Account is shown on Form 88 (see p. 670).

The following are the liquidator's affidavits for his accounts as prescribed by the Companies Winding-up Rules, 1909—

No. 87. (Rule 170.)

AFFIDAVIT VERIFYING LIQUIDATOR'S ACCOUNT
UNDER SECTION 155

(Title.)

I, G. H., of , the Liquidator of the above-named company, make oath and say—

That * the account hereunto annexed marked B contains a full and true account of my receipts and payments in the winding up of the above-named company from the day of , 19 , to the day of , 19 , inclusive * and that I have not, nor has any other person by my order or for my use, during such period received any moneys on account of the said company * other than and except the items mentioned and specified in the said account.

Sworn at, etc. }

* NOTE.—If no receipts or payments, strike out the words in italics.

No. 88A. (Rule 171.)

AFFIDAVIT VERIFYING
LIQUIDATOR'S TRADING ACCOUNT UNDER
SECTION 155

(Title.)

I, _____, the liquidator of the above-named company, make oath and say that the account hereto annexed is a full, true, and complete account of all money received and paid by me or by any person on my behalf in respect of the carrying on of the trade or business of the company, and that the sums paid by me as set out in such account have, as I believe, been necessarily expended in carrying on such trade or business.

Sworn, etc.

Liquidator.

(l) **Taxation of Bills.** Every solicitor, manager, accountant, auctioneer, broker or other person employed by a liquidator must on request by the liquidator, to be made a sufficient time before the declaration of a dividend, deliver his bill of costs or charges for taxation, and if he fails to do so within the time stated, or such extended time as the Court may allow, the liquidator may declare and distribute the dividend without regard to such person's claim, and, subject to any order of the Court, the claim shall be forfeited.

Before any bill is taxed, a certificate of employment signed by the liquidator and stating what (if any) special terms of remuneration have been agreed upon, must be produced to the taxing officer, and also when necessary a copy of the resolution or other authority sanctioning the employment.

No payments in respect of bills or charges of solicitors, managers, accountants, auctioneers, brokers, etc. (other than costs of preparing a Statement of Affairs when sanctioned by the Official Receiver) will be allowed till they have been considered and allowed by the Registrar. The taxing-master must satisfy himself that the employment was duly sanctioned.

The following is the official form of request to deliver bills for taxation as prescribed by the Companies Winding-up Rules, 1909.

No. 89. (Rule 177.)

REQUEST TO DELIVER BILL FOR TAXATION

(Title.)

I hereby request that you will, within _____ days of this date, or such further time as the Court may allow, deliver to me for taxation by the proper officer your bill of costs [or charges] as (a) _____ failing which, I shall, in pursuance of the Companies (Consolidation) Act and Rules proceed to declare and distribute a dividend without regard to any claim which you may have against the assets of the Company, and your claim against the assets of the Company will be liable to be forfeited.

Dated this _____ day of _____, 19 _____.

(a) Here state nature of employment.

(l) **Returns under Section 224, Companies (Consolidation) Act, 1908.** The returns to the Board of Trade under Section 224, as referred to under the heading of *Voluntary Liquidation*, p. 644, are required to be made in compulsory liquidation.

All unclaimed dividends or assets of the company which have, according to the return, remained undistributed for six months after the date of receipt must forthwith be paid into the Companies Liquidation Account at the Bank of England.

For the purpose of Section 224 the conclusion of the winding up is to be taken in compulsory liquidation as either the date on which the order dissolving the company has been returned by the liquidator to the Registrar of Companies, or the date of the order of the Board of Trade releasing the liquidator.

(m) **The Release of the Liquidator.** When the liquidator has realised all the property of the company, or so much thereof as can, in his opinion, be realised without needlessly protracting the liquidation, and distributed a final dividend, if any, to the creditors, and the rights of the contributories between themselves have been adjusted, and he has made a final return, if any, to the contributories, or has resigned, or has been removed from his office, he may apply for his release.

Before doing so he must give notice of his intention to do so to all creditors who have proved their debts, and to all the contributories, and send with the notice a summary of his receipts and payments as liquidator.

The Board of Trade, on his application, causes a report on his accounts to be prepared, and on his complying with all its requirements, takes into consideration the report, and any objection which may be urged by any creditor or contributory, or person interested against the release, and must either grant or withhold his release; subject to appeal to the Court.

If the release is withheld the Court may make such order as it thinks just, charging the liquidator with the consequences of any act or default he may have done or made contrary to his duty.

The release operates as a removal of the liquidator from his office; and discharges him from all liability in respect of any act done or default made by him in the administration of the affairs of the company, or otherwise in relation to his conduct as liquidator; but such order may be revoked on proof that it was obtained by fraud or by suppression or concealment of any material fact.

Notice of the Board of Trade order granting release is gazetted; the liquidator provides the stamp and charges it against the company's assets.

The release does not take effect till all books and documents have been handed over to the Official Receiver.

The release must be obtained if the liquidator vacates his office for *any* reason; therefore if the vacancy occurs through death the legal personal representative must obtain the release, in order to free the estate of the deceased from liability.

The following are the official forms, including the summary of receipts and payments, under the Companies Winding-up Rules, 1909, relating to the application for release.

No. 98. (Rule 197.)

NOTICE TO CREDITORS AND CONTRIBUTORIES
OF INTENTION TO APPLY FOR RELEASE

(Title.)

Take notice that I, the undersigned liquidator of the above-named Company, intend to apply to the Board of Trade for my release, and further take notice that any objection you may have to the granting of my release must be notified to the Board of Trade within twenty-one days of the date hereof.

A summary of my receipts and payments as liquidator is hereto annexed.

Dated this day of , 19 .
Liquidator.

To

NOTE.—Section 157 (3) of the Companies (Consolidation) Act, 1908, enacts that "An order of the Board releasing the liquidator shall discharge him from all liability in respect of any act done or default made by him in the administration of the affairs of the Company, or otherwise in relation to his conduct as liquidator, but any such order may be revoked on proof that it was obtained by fraud or by suppression or concealment of any material fact."

No. 99. (Rule 197.)

APPLICATION BY LIQUIDATOR
TO BOARD OF TRADE FOR RELEASE

(Title.)

I, the liquidator of the above-named Company, do hereby report to the Board of Trade as follows—

1. That the whole of the property of the Company has been realised for the benefit of the creditors and contributories [and a dividend to the amount of

shillings in the pound has been paid as shown by the statement hereunto annexed, and a return of per share has been made to the contributories of the Company];

[or That so much of the property of the Company as can, according to the joint opinion of myself and the Committee of Inspection, hereunto annexed, in writing under our hands, be realised without needlessly protracting the liquidation, has been realised, as shown by the statement hereunto annexed, and a dividend to the amount of shillings has been paid, together with a return of per share to the contributories of the Company]; (a)

2. I therefore request the Board of Trade to cause a report on my accounts to be prepared, and to grant me a certificate of release.

Dated this day of , 19 .
Liquidator.

(a) Add, if necessary, "That the rights of the contributories between themselves have been adjusted."

(n) **Special Manager's Accounts.** During the time the Official Receiver is acting as liquidator and also if he permanently continues to act as liquidator a special manager may be appointed by the Court upon the application of the Official Receiver, when he is satisfied that the nature or state of the business of the company or the interests of the creditors or contributories require it.

The special manager must record his receipts and payment and account to the Official Receiver, and he receives such remuneration as the Court, upon the recommendation of the Official Receiver, directs.

The accounts of the special manager must be verified by affidavit and when approved by the Official Receiver, the account of his receipts and payments will be added by the Official Receiver to his accounts.

LLOYD'S BONDS.

Bonds introduced to evade the Mortgage Debenture Act, which are so called from the name of the counsel who first settled the form of the bond. By the Mortgage Debenture Act a company is prohibited from borrowing more than an amount equal to two-thirds of its paid-up capital. The bonds are in the form of ordinary promissory notes, bearing interest payable to bearer. As between the company and the first holder they are void, as commercial frauds, and the first holder, being a party to the fraud, cannot recover either principal or interest. But if a first holder possesses such bonds for value, the subsequent holder, being an innocent party, is entitled just as if it was an ordinary bill transaction. This legal fiction has been upheld entirely by the courts.

LOAN CAPITAL.

Although often heard in connection with the finance of a limited company to designate the money received in connection with debenture issues, this term, used in this manner, is not quite correct, as, strictly speaking, loans do not form any part of the company's capital. The expression, however, is frequently met with, and in the Finance Act, 1899, loan capital includes any debenture stock, county stock, corporation stock, municipal stock, or funded debt, by whatever name known, or any capital raised by any local authority, corporation, or company, which is borrowed or has the character of borrowed money.

LOAN CREDITOR.

A person who has lent money is a loan creditor of the borrower.

LOAN LEDGER.

(See AUDITING, p. 99.)

LOAN ON MORTGAGE.

In the books of the business to which the loan is advanced, the lender will be credited and the

loan will appear as a liability in the Balance Sheet. A memorandum should be placed upon the Balance Sheet immediately under the asset hypothecated, drawing attention to the existence of the advance on mortgage appearing amongst the liabilities. The auditor will, of course, see that the advance is actually received, and, in the case of joint stock companies, will examine the Mortgage Register to see that the correct particulars of the mortgage are entered therein. He should also require the production of a duly verified copy of the Mortgage Deed in order to ascertain the property charged, the rate of interest payable, and the time and terms of repayment, and he should examine the Articles of Association to see that borrowing powers exist and are not exceeded.

In the books of the lender the advance will be debited to the borrower and shown in the Balance Sheet as an asset. The amount of the advance will be vouched by the production of the Mortgage Bond and Deeds to the auditor. If the advance be made to a joint stock company, the auditor should satisfy himself as to the company's power to borrow the money, and as to the proper registration of the mortgage with the Registrar of Joint Stock Companies. He should further see that proper provision is made for the safe custody of the Mortgage Bond and any title deeds that accompany it. He will also vouch the regular receipt of interest and see that the terms of repayment are duly carried out.

LOANS.

(See AUDITING, p. 88; BALANCE SHEET, p. 145.)

LOANS FROM BANKERS.

(See AUDITING, p. 105.)

LOANS, OVERDUE ACCOUNTS.

(See OVERDUE ACCOUNTS, LOANS.)

LOCKE KING'S ACT.

This Act was passed in 1854, and has been extended by two subsequent Acts, passed in 1867 and 1877 respectively. The three are now known under the name of the Real Estates Charges Acts. The effect of the Acts is shortly as follows: When a person dies possessed of any landed property—freehold, copyhold, or leasehold—and the property is subject to any mortgage or charge, or to a vendor's lien for unpaid purchase money, or other equitable charge, and the property is devised to or devolves upon any particular person, such person takes the property burdened with the charge to which it is subject. Prior to the first of the Acts referred to above, there was always a right to demand that the charge should be paid off out of the personal estate of the deceased.

LONDON GAZETTE.

The official paper published by the authority of the Government and containing all notices of

importance connected with administrative matters. In addition, all the principal steps taken in bankruptcy and in the winding up of joint stock companies, all notices of charges in partnerships, and all notifications calling upon creditors and others to come in and prove their claims in the administration of estates must be advertised in the *Gazette*. The paper is published twice a week, on Tuesdays and Fridays, though it is not impossible for special editions to be issued under particular circumstances.

LOOSE-LEAF LEDGERS.

The Loose-leaf Ledger, sometimes called the Perpetual Ledger, has met with a more ready acceptance than the Card Ledger, and for ordinary book-keeping purposes, is generally considered more serviceable, although, at first, counting-house conservatism showed considerable opposition to its introduction.

It has many qualities in common with the Card Ledger, but being in book form, and being capable of use when in a locked state, it appeals more readily to those responsible for counting-house management.

The leaves bearing the accounts are secured in the covers of the ledger by means of either leather thongs or steel rods, and the ledger can be locked so that it is impossible to remove a leaf while the ledger is in that condition. The covers are made of very durable materials, and the leaves of strong superior paper. As the leaves become full, or when an account is closed, they are removed from the ledger and placed in a Transfer Ledger, this latter being a case of similar mechanism to the ledger, but generally made of less substantial materials. There then remain in the ledger only the "open," "live," or "operative" accounts.

In the Loose-leaf Ledger the index runs throughout the book, accounts commencing with the same initial letter being grouped together and divided from the next letter by a guide sheet having the initial letter printed upon a projecting tab. Each guide sheet constitutes a numerical index for its respective letter—thus, on the guide sheet "A" would be entered up the index for the accounts in the A group. Each account has a separate sheet and number, and the accounts in each group are placed in the ledger in numerical order.

When an account has been filled up, another sheet has to be substituted for it; the substituted sheet receiving the same account number, but a progressive sheet number. Thus, suppose James Anderson's account is number 16, and the first sheet is completely filled up, the continuation sheet of the account is numbered "Account 16, sheet 2," and the third one, when put in use, "Account 16, sheet 3." James Anderson's account is always the same number, viz., 16, but may in course of time consist of many sheets, all of which would,

with the exception of the operative current sheet, be in the Transfer Ledger under the letter A and in proper numerical location.

It is advisable for a responsible official to have under his charge, not only the stock of supply sheets, but also the key of the ledger, the object being to minimise the risk of manipulation or substitution of sheets. Many users have the sheets not only specially numbered for stock purposes, but also privately marked.

ADVANTAGES.—The following advantages are claimed for the Loose-leaf Ledger—

1. Each account has a definite place and number assigned to it, and consequently the book-keeper can locate its position with the least possible loss of time. In the bound book ledger, an account may be spread over many differently numbered pages in different parts of the ledger or ledgers, owing to the space originally allocated to it not being sufficient.

2. When a ledger account is once opened, it is opened for all time, and there is no writing up of new ledgers and consequent "guessing" of the number of pages or space to be allowed for the account.

3. The index is a "permanent" one, and the writing up of new indexes (necessary when a new bound book ledger is opened) is obviated.

4. The position and number of a ledger account never change, and in consequence the book-keeper very quickly memorises the accounts, and recourse to the index is seldom necessary.

5. All old matter can be removed from the ledger, and nothing but "live" or "operative" accounts retained, whereas in the bound book ledger, "dead" matter remains so long as the book is in use.

6. The complete records of each customer's account are kept together, and not scattered over many positions in several ledgers.

7. The classification of accounts can be effected with the avoidance of waste of space.

8. There are no blank leaves, and this secures the minimum of waste. In the bound book ledger many leaves are unwritten upon at the time when a new ledger becomes a necessity.

9. In compiling a list of open ledger balances, there is no waste of time in turning over pages of dead matter.

10. It is less cumbersome and more easily worked than the Card Ledger.

By an official, other than the ledger clerk, keeping control of the supply sheets and ledger key, the chief disadvantage—the manipulation of leaves for dishonest purposes—is overcome.

It is not absolutely necessary to enter up the names of the accounts in the index, or to number the accounts. By placing each account in strict alphabetical order and in its own index sub-division, account numbers may be dispensed with, although

the sheet numbers of the accounts would be retained. Thus, the first sheet used for John Smith's account would be sheet No. 1, and when that sheet has been fully written up, the next sheet used for John Smith would be sheet No. 2, and so on.

Nor is it absolutely necessary for the ledger ruling to be the ordinary debit and credit account form. The loose-leaf principle may be employed in the case of tabular ledgers. Take, for example, the tabular ledger now generally in use in the laundry industry. The one great disadvantage that this ledger has is the necessity for frequent re-writing of the customers' names and the carrying forward of the balances to a new portion of the ledger. This has in the Loose-leaf System been overcome by the use of sheets of different width.

Upon the wider (or index) sheets are written the customers' names. The narrower sheets are ruled with the tabular money columns only. When the money columns are all used up and it is necessary to "carry forward" to fresh leaves, the ledger is unlocked, the completed leaves removed, and fresh blank ones inserted. The wide index leaves, containing the customers' names and addresses, are retained in the ledger, and are removed only when they become too dilapidated for further use. The leaves may be classified in journeys and the accounts for each journey kept in alphabetical order—no two different initial letters being upon one sheet. The A's are thus kept together, then the B's, and so on, each letter having leaves for itself. The first complement of narrow leaves would be marked—

A 1 } A 2 } A 3 } B 1 } B 2 } B 3 }
sheet 1 } sheet 1 } sheet 1 } sheet 1 } sheet 1 } sheet 1 }

etc.; while the second complement would be marked—

A 1 } A 2 } A 3 } B 1 } B 2 }
sheet 2 } sheet 2 } sheet 2 } sheet 2 } sheet 2 }

and so on.

Not only are the leaves numbered, but the lines down the page are numbered also—the lines being the customers' accounts. The corresponding lines on the narrow sheets are numbered to agree, so that line 9 on the narrow sheet will fall flush with line numbered 9 upon the wide index sheet.

When the leaves are completed and have to be removed to the transfer binder, they are arranged in alphabetical numerical order; thus, leaves A 1 would be placed with their successive sheets before leaves A 2, then the sheets of A 2 would follow before A 3.

It will consequently be seen that by reference to the transfer binder, a complete unbroken record of any customer's account can be obtained. In

the case of the bound laundry ledger, the preparation of a complete record of any customer's account necessitates the abstraction of details from many different portions of many different ledgers, and is a matter which absorbs much valuable time.

For a Prime Cost Ledger or Contracts Ledger, the loose-leaf principle is exceptionally serviceable. The ledger proper, containing current contracts alone, is always in workable compass, and in the transfer binder all details for each completed contract are to be found in one position and not scattered over numerous portions of a book, or perhaps several books.

LOOSE PLANT AND TOOLS.

Purchases of loose plant and tools should be debited through the medium of the Invoice Analysis Book to a Loose Tools Account.

The tools and plant on hand should be entered in an inventory at stocktaking and revalued, and the valuation credited to the Loose Tools Account, the balance of the account then being charged against revenue. After several periods of revaluation the experience may, if it be desired, be used to determine the rate of depreciation, and the rate so fixed applied in writing down the asset in future : but the system of periodical revaluation is preferable.

An inventory of loose plant and tools should be kept, in which all new loose tools and plant purchased, should be recorded. The inventory should be provided with columns for recording each successive valuation at stocktaking times, and all plant and tools sold or otherwise disposed of should be regularly marked off. In addition to this, a separate inventory should be made of the plant and tools actually on hand at stocktaking, which should be compared with the permanent inventory or register. Discrepancies should be inquired into, and it will be the duty of the auditor periodically to make this comparison himself, so that he may be satisfied that no plant or tools are included in the valuation which are not actually in the possession of the business at stocktaking.

LOSS ON REALISED SECURITIES.

(See PROFIT AND LOSS ACCOUNT, p. 793.)

LOSS OR DAMAGE BY FIRE OR WATER.

The treatment of losses or damage by fire or water depends upon the nature of the loss or damage suffered. In the case of loss of stock, where insured, the amount received or receivable from the insurance company may be credited to an appropriate account, and subsequently may be transferred to the Trading Account. If uninsured, the loss will automatically adjust itself when the accounts are prepared subsequently,

simply because of the omission of the lost stock from the sales or closing stock of the period. In such a case, if it is desired to ascertain the amount of loss attributable to the fire, a Stock Account should be prepared, which should be debited with the opening stock of the period, the purchases made, the wages and direct charges (in the case of a manufacturing business) and the gross profit calculated upon the sales made, at the average rate as ascertained by experience. The account will then be credited with the actual sales made and the actual stock on hand, and the balance then remaining to the debit of the account will approximately represent the loss suffered.

In the case of the loss of buildings, plant, or other capital items, the damage suffered should be ascertained by the fire assessors. The assessment made by them should be credited to the appropriate Capital Account and, if uninsured, debited to the Profit and Loss Account. In the case of loss of insured property, the sum received or receivable should be credited to the Capital Account and the insurers debited.

The auditor should direct his attention to ascertaining that the full amount of the loss suffered is brought into account. He should satisfy himself (1) that a proper apportionment of the loss between capital and revenue is made, (2) that no claim un-admitted by the insurance company is credited to revenue (a reserve in the case of dispute is advisable), (3) that in the event of under-insurance, the whole of the loss is credited in the Capital Accounts and the irrecoverable portion debited to Profit and Loss Account, and (4) that no damaged matter, or salvage, is subsequently taken into stock as perfect.

LOST BILL.

When the holder of a bill of exchange, cheque, or promissory note loses it, or if it is accidentally destroyed, the parties liable upon it are not thereby necessarily discharged from their obligations. Under such circumstances the loser is entitled to demand a new bill of the same tenor as the lost one from the drawer, provided the demand is made before the bill is overdue. The drawer, however, can refuse to accede to such a demand unless he receives an adequate indemnity to reimburse him in case the original is discovered and negotiated. When an action is brought in respect of a bill, the Court may order that the loss of the instrument shall not be set up as a defence, provided that a satisfactory indemnity has been given. (See also BILL OF EXCHANGE.)

LUNACY COMMISSION.

(See COMMISSION IN LUNACY.)

LUNAR MONTH.

A period of twenty-eight days. In law the word "month" always means "lunar month,"

unless there is some statutory enactment which makes its meaning "calendar month," such as in the case of the Bills of Exchange Act, 1882, and the Sale of Goods Act, 1893, or unless, according to the ordinary rules of construction of documents, a secondary meaning can be admitted. (See also MONTH.)

LUNATIC.

A person of unsound mind. Such a person is under a disability as to contracts; but it is to be remembered that the contract entered into is only voidable, and not absolutely void, although in any case the estate of the lunatic is liable for the reasonable price of necessities supplied. In order, however, that a lunatic, or rather his

committee, may exercise the right of repudiation of any contract entered into by the lunatic during an insane period, it must be shown that the other party to the contract was ignorant of the lunatic's mental condition at the time when the contract was entered into. This was clearly set out in the case of the *Imperial Loan Company v. Stone*, 1892, 1 Q.B. 599. During a lucid interval a lunatic has the same contractual capacity as any other person. He may also ratify, during his period of sanity, any contract entered into whilst he was insane.

The committee of a lunatic is the person (or sometimes the persons, for in certain cases more than one may be appointed) to whom the care of a lunatic's person and property are confided. The person chosen is generally a person who is near of kin to the lunatic.

MACHINERY, DEPRECIATION OF.

(SEE DEPRECIATION, p. 405.)

MACHINES AND APPLIANCES, OFFICE.

(SEE OFFICE MACHINES AND APPLIANCES.)

MAINTENANCE.

It is a principle generally recognised in any system of jurisprudence that if an action at law has to be taken, only the person aggrieved can move in the matter. Of course, if this person is under any legal disability, proceedings may be instituted by certain persons who are empowered by various statutes to act in substitution for him. In the same way, the person against whom action is taken can alone appear in the courts to defend the claim made against him. The officious interference of third parties on behalf of either a plaintiff or a defendant, when that interference takes the form of supplying money to provide for costs, etc., is called maintenance. An exception may be made when the party to the suit and the party rendering assistance are related to each other, or where the help that is rendered is afforded on charitable grounds. Otherwise maintenance is a misdemeanour, and may be punished by fine or imprisonment. This offence is to be distinguished from champerty (*q.v.*), which is an agreement to share the proceeds of a law suit, and barratry, of which it is sufficient to say that it consists in stirring up strife and quarrels amongst the King's subjects. Each of these is, like maintenance, a misdemeanour and punishable in the same way, that is, by fine or imprisonment.

MAINTENANCE RESERVE ACCOUNT.

An account raised in order to prevent unequal amounts being charged against annual Profit and Loss Accounts in respect of repairs and upkeep, such amounts being placed to the credit of the account each year, and debited against Profit and Loss Account. These amounts, as experience teaches, represent the equalised annual charge to maintain the assets of the undertaking in a working condition. The repairs and upkeep are then debited to the account, and thus the reserve so created is taken advantage of when the amount expended in any year exceeds the equalised annual charge.

MALA FIDES.

(SEE GOOD FAITH.)

MALA IN SE.

All things which are evil in themselves are thus termed, in contradistinction to those things which are only forbidden by the laws of the country, and which are called *mala prohibita*, that is, forbidden evils. Instead of *mala prohibita* the phrase *mala quia prohibita* is sometimes used.

MALA PROHIBITA.

(SEE MALA IN SE.)

MALFEASANCE.

This is a legal term which, although often confounded with misfeasance (*q.v.*), is limited more correctly to the doing of a wrongful act, the other term, misfeasance, being confined to the doing of a lawful act in a wrongful manner. A corporate body, like an individual, is liable for all acts of malfeasance and misfeasance. (SEE ALSO NONFEASANCE.)

MANAGEMENT EXPENSES.

(SEE PROFIT AND LOSS ACCOUNT, p. 790.)

MANAGING DIRECTOR'S SALARY OR OTHER REMUNERATION.

Where a salary is paid to a managing director, a separate account for the record of the payments to him should be opened in the Ledger, and all the payments made duly debited therein. The auditor, should, in the first place, refer to the Articles of Association to ascertain whether they fix the amount or limit of the managing director's salary, or whether they confer upon the directors the power to appoint a managing director and to fix his remuneration. In the latter event, further reference should be made to the Directors' Minute Book for the minute fixing the appointment and salary. The auditor should assure himself that the meeting was a properly convened and properly constituted one. He should note that the sum actually paid agrees with the authorised sum, and should verify the payments by requiring the production of receipts properly stamped and signed by the managing director.

MANDAMUS.

This is a Latin word meaning "we command." It is a writ issued by the High Court of Justice against an official or a public body commanding him or them to do a certain thing, which it is his or their duty to perform. The method of procedure is as follows. The person or body aggrieved

applies *ex parte* to a Divisional Court of the High Court, supporting his application by an affidavit setting out the nature of the case, and if the court is satisfied that there is a *prima facie* cause of complaint, a rule *nisi* is granted, and in due course the respondent must appear and show cause why the rule *nisi* should not be made absolute and a writ of mandamus granted. It is upon this second hearing that the case is fully threshed out and the decision of the court given as to the matter in dispute. The opposite of a writ of mandamus is a writ of prohibition (*q.v.*), which is directed to a person or to a public body ordering him or them to refrain from doing a certain thing. The procedure is the same in applying for a writ of prohibition as in applying for a writ of mandamus.

MANUFACTURING ACCOUNT.

An account raised to give the cost of manufacture, and, therefore, debited with materials used, wages paid, and rent., etc., of factory, carriage, royalties, repairs to machinery, and depreciation of same, and any other items expended in the production of the goods. The account is credited with sales, the balance showing the gross profit of manufacturing. (See also COST ACCOUNTS.)

MANUFACTURING CHARGES.

These charges include all direct factory charges, such as wages, factory managers' salaries, factory rent, rates and taxes, and the cost of fuel. Carriage inwards, being a part of the cost of the purchases of raw material, is also a manufacturing charge, and, along with the other charges, should be debited to the Manufacturing Account.

The auditor will see that only appropriate charges are included in this account, and, where an apportionment of several establishment expenses is made, he will assure himself that the basis of apportionment is an equitable one.

MANUFACTURING WAGES.

The wages of workmen engaged directly upon the productive side of the business, as distinct from the wages of employees engaged on the distributive side, should be charged against the Manufacturing Account.

In order to verify the charge, the auditor should require the production of the analysis of wages paid, in which the names of the productive employees and the amounts paid to them should be set out in detail, and should satisfy himself that the same efficient internal check is in existence, and apply the same tests to prove the accuracy of the manufacturing wages, as in the case of all classes of wages.

MARINE INSURANCE FUND.

The creation of a Marine Insurance Fund is only possible when a fleet of ships is owned, so that there is an opportunity of averaging the

risks over the whole fleet. Contributions to the fund should be determined by the rates payable to outside insurers in respect of the risks. A sum equal to, or possibly in excess of, the premiums which would be payable should be credited to the Marine Insurance Fund, and the various Voyage Accounts should be debited with their respective proportions of the contributions to the fund. The sum so set aside should be invested outside the business in well-secured and easily realisable investments, so that they may be readily available if required. The interest arising from such securities, together with all sums received from salvages, etc., should be credited to the fund. The cost of re-insurances, the expenses of administering the fund, and losses arising on the risks insured should be debited to the fund. Losses arising by depreciation of investments may also be charged to the fund, although, until the fund is firmly established, it is preferable to make good such losses out of revenue.

In verifying this form of reserve, an auditor should satisfy himself that the contributions to the fund are adequate, that the interest on investments is duly received and credited to the fund, and that all expenses and losses properly chargeable to the fund are so dealt with. He will verify the existence of the investments by an examination of the securities held; or, in the case of inscribed stock, by obtaining certificates from the banks in whose books the stock is registered.

MARITAL CONTROL.

According to the common law a woman was almost entirely under the control of, or subservient to, her husband in respect of her property. This control has been almost entirely abolished by reason of the various Married Women's Property Acts. (See MARRIED WOMAN.)

MARKET OVERT.

The meaning of this term is "open market," and it becomes of importance when a purchaser has bought goods from one person who is not the rightful owner, for although no lapse of time gives a good title, in the ordinary course of things, to the possessor of goods which have been stolen, a purchase in market overt may constitute an exception.

It is a well-known maxim of law that no man can give that which he does not possess—*nemo dat quod non habet*. Therefore, in the case of any transfer, by sale or otherwise, the transferee of property only gets the title which the transferor had. Consequently, if the transferor's title was bad, that of the transferee is also bad, and the rightful owner may claim the return of his property at any time, no matter in whose possession it may be. To this rule, however, there are

exceptions, provided the transactions are carried out *bona fide*. Thus, if a factor or agent is invested with proper authority to deal with the goods, the purchaser will get a good title. The same applies when the subject-matter is a negotiable instrument. And last of all these exceptions is the case of a sale in market overt, when, provided everything is done in good faith, the purchaser of an article which is tainted in any way, so far as title is concerned, will obtain an absolute right to the same even though he purchases it from the actual thief, and the rightful owner cannot reclaim the article after such a sale, unless the thief is prosecuted and convicted. If there is no prosecution, and consequently no conviction, the article, although stolen, remains the property of the purchaser. It is to be noticed, however, that this re-vesting of the property does not take place if the article purchased has been obtained in the first instance from the rightful owner by wrongful means not amounting to a felony, such as, for example, by false pretences.

Market overt means an open or public market as distinguished from a place for private sale. In the country, market overt is only held on the special days provided for the particular town by charter or by long usage, and only in the special place set apart for the holding of the market. In the City of London, every day, except Sunday, is market day, and every shop in which goods are publicly exposed for sale is market overt for such things as the shopkeeper professes to deal in. Some provincial towns have special privileges as to market overt, but these must be gathered locally. Good faith is an essential in connection with all transactions carried out in market overt, and the goods sold must be actually exposed. For example, a sale by sample is not a sale in market overt. And when it is the case of a sale in a shop which has the privilege of market overt, any transaction must take place in the public part of the shop and not in any back room or out-of-the-way place. It would appear that the benefit of market overt cannot be claimed by the shopkeeper, if the shop is market overt, when he is the purchaser and not the seller of the goods dealt in.

The re-vesting of the property in goods which have been stolen is provided for by the Larceny Act, 1861, and the Sale of Goods Act, 1893, the latter Act having introduced the exception, in the case of a sale in market overt, to their re-vesting, even if the person who has unlawfully obtained them has been prosecuted and convicted, when the goods have been obtained otherwise than by a felony. This exception has already been noticed.

Sale in market overt applies to goods, wares, and merchandise only. It has no reference to land, and it does not affect securities. The sale

of horses in open market is provided for by special legislation.

MARRIAGE SETTLEMENTS.

These are settlements made before or after marriage, by which certain property is tied up in trust for the persons who are to be married, or who have been married, and their descendants, or upon such other persons as are contemplated at the time of the making of the settlements.

A marriage settlement is either ante-nuptial or post-nuptial. If it is ante-nuptial, that is, made before the date of the marriage, it is always valid, unless tainted with fraud, since marriage is a valuable consideration, and the settled funds or property cannot be attached in the case of the bankruptcy of those who are life tenants under the settlement. If, on the other hand, it is post-nuptial, that is, made after the date of the marriage, the settlement is absolutely void in favour of creditors of the person who has provided the settled funds, if such person is made bankrupt within two years of the date of the settlement, or within ten years, unless it is proved that at the time of the making of the settlement the bankrupt was quite solvent without taking into account the property brought into the settlement. It is only against the trustee in bankruptcy, however, that the settlement is void or voidable. As between the parties to the settlement, it is perfectly valid.

The settled funds may be provided from various sources—from the husband or from the wife, or from both, or from an independent source. But the object is always the same, namely, to vest certain property in trustees, to provide for the husband and wife during their lives, and to hold the whole in trust for the children of the marriage or more remote descendants, so far as is allowed by the law against perpetuities (*q.v.*), provision always being made to meet the case where there are no children or descendants, by naming the persons or class of persons amongst whom the property is to be divided ultimately.

It would be impossible to enter into details as to the form of a marriage settlement, as so much must depend upon the source or sources from which the settled property is derived. And again, there is a great difference between a "strict" settlement, that is, one which is concerned with real property, and a settlement "by way of trust," which applies to both real and personal property. The proper course is for the parties to the marriage, or those outside persons who may perchance provide the settled funds, to declare their intention as to the manner in which they desire the income arising from the property and the final destination of the same to be dealt with, and then to leave the matter to the practical conveyancer to frame the marriage settlement upon the lines indicated by them.

The parties to a contract must not, generally speaking, be minors. There is, however, an exception to the rule in the case of marriage settlements. By the Infants Settlement Act, 1855, infants not being under twenty years of age, if males, or seventeen, if females, may, with the approbation of the court, make binding settlements of their real and personal estate, in possession or otherwise, on their marriage. The court may, under the same Act, direct a settlement of an infant's property after marriage, but it has no power to compel a ward of court to make a settlement.

MARRIED WOMAN.

Except in so far as she has been emancipated by modern legislation, a married woman is still to be regarded as a person under disability in certain respects. It is often erroneously assumed that a married woman has attained the position occupied by a *feme sole*, that is, a spinster or a widow. This is altogether inaccurate, and in point of fact a married woman only enjoys the rights and escapes the liabilities of the ordinary individual to the extent which the legislature has thought fit to allow.

At common law, a married woman had no power of contracting whatever, subject to certain exceptions in which she was held to be contracting as the agent of her husband. This rule of law was changed altogether by the Married Women's Property Act, 1882, supplemented by the Married Women's Property Act, 1893. By Section 1, Subsection 2, of the former Act, it is provided that "a married woman shall be capable of entering into and rendering herself liable in respect of and to the extent of her separate property on any contract, and of suing and being sued, either in contract or in tort or otherwise, in all respects as if she were a *feme sole*, and her husband need not be joined with her as a plaintiff or defendant, or be made a party to any action or other legal proceedings brought by or taken against her; any damages or costs recovered by her in any such action or proceeding shall be her separate property, and any damages or costs recovered against her in any such action or proceeding shall be payable out of her separate property and not otherwise." By Section 1 of the latter Act, it is provided that "every contract hereafter entered into by a married woman otherwise than as agent (a) shall be deemed to be a contract entered into by her with respect to, and to bind, her separate property, whether she is, or is not, in fact possessed of, or entitled to, any separate property at the time when she enters into such contract, (b) shall bind all separate property which she may at any time or thereafter be possessed of or entitled to, and (c) shall be enforceable by process of law against all property which she may thereafter, while discover-

be possessed of or entitled to; provided that nothing in this section contained shall render available to satisfy any liability or obligation arising out of such contract, any separate property which at that time or thereafter she is restrained from anticipating." There is one more special Act in reference to married women, passed in 1907, which gives them certain powers to act independently of their husbands when they are sole trustees under a will or settlement, but this needs no further mention here.

The result of this modern legislation has been to place married women in a position similar to that occupied by those who are unmarried with these reservations, (1) they cannot contract personally, but only in respect of their separate estate, and (2) they cannot bind that separate estate which they are restrained from anticipating. (See RESTRAINT ON ANTICIPATION.) If, therefore, a married woman enters into a contract, the remedy of her creditor is confined to her separate estate, and there is no remedy against her personally. When judgment is obtained against her, the judgment creditor can only proceed against her separate estate, and if she has no such separate estate he has no remedy. She cannot be committed upon a judgment summons, except in respect of contracts entered into before marriage, or of torts committed during marriage, and when a judgment is obtained against her whilst she is a married woman, the death of her husband does not convert the judgment into a final judgment upon which she can be made personally liable.

By the Bankruptcy Act, 1914, a married woman is subject to the bankruptcy laws if she carries on a trade or business, whether separately from her husband or not, as though she was a *feme sole*; and the court may in such a case even attach the whole or a part of her private income, even though the same is subject to a restraint on anticipation. But unless she is engaged in trade, a married woman cannot be made a bankrupt.

A married woman has the same power of contracting with her husband as with any other person in respect of her separate property, and by Section 12 of the Act of 1882, the wife has the same civil remedies against all persons, including her husband, for the protection and security of her separate property, as if such property belonged to her as a *feme sole*. The husband occupies a somewhat different position so far as procedure is concerned, though the result is practically the same.

When husband and wife are living together, the wife has an implied authority to bind her husband for necessities for herself and in household affairs generally. This she does as the agent of her husband. But since the agency is only an implied one, the husband may rebut any presumption against him by showing that he has forbidden his wife to pledge his credit. But this will not be

sufficient in the case of those tradesmen with whom the wife has had dealings and who have treated her as her husband's agent with his implied assent. In addition to forbidding his wife to pledge his credit, the husband must give information to the particular tradesmen that the agency is withdrawn. And in cases of difficulties, the *onus* will be upon the husband to prove that the withdrawal of the agency has actually come to the knowledge of these tradesmen. Merely inserting an advertisement in a newspaper is of no real value. Any tradesman dealing with the wife for the first time, must take his chance. If a married woman has been forbidden by her husband to pledge his credit, and then goes to a tradesman and orders goods—this being a first transaction—the husband is in no way liable, since there is no question of agency; and unless the married woman has any separate property, the tradesman is legally without any remedy.

As to torts committed by a married woman, the husband is still liable in respect of the same at common law, if husband and wife are living together, and the husband may be sued either jointly with his wife, or alone, in any claim for damages made by the injured party.

The peculiar immunity of a married woman in respect of contracts comes to an end with the termination of the marriage tie. This is very frequently forgotten by all parties. Unmarried, whether as a spinster or as a widow, the woman occupies the same position as a man in a contractual sense. It is only when she is actually a married woman that she is specially protected. But even when married she does not escape liability for her ante-nuptial debts. For these she is always liable, married or unmarried, subject, of course, to such defences as infancy, or the Statutes of Limitations, which must be specially pleaded in an action.

MARSHALLING THE ASSETS.

This means applying the assets in the prescribed order for payment of debts where the assets are sufficient for the payment of all debts but not sufficient to pay all legacies, devises, etc. The order is as follows—

- (1) Residue of general personalty.
- (2) Real estate devised for payment of debts.
- (3) Realty descended to the heir.
- (4) Realty or personalty devised or bequeathed subject to payment of debts.
- (5) General pecuniary legacies.
- (6) Specific devises, residuary devises, and specific bequests not charged with payment of debts.
- (7) Realty and personalty appointed by will under a general power of appointment.
- (8) Paraphernalia of the widow.

(See also EXECUTORSHIP ACCOUNTS, p. 449.)

MATERIALS CONSUMED.

In order to ascertain the quantities of materials consumed in manufacturing concerns, it is necessary that the various materials accounts should be debited (1) with the purchases and (2) with the stock of material on hand at the beginning of the trading period, and credited with the stock on hand at its close. The balance on the account will then represent the value of materials consumed.

The auditor should verify the stock entries in the accounts by reference to the stock lists, which, in their turn, will have been duly vouched. (See STOCK-IN-TRADE.)

Materials consumed should be charged against the manufacturing account. The amount of material consumed should bear a constant proportion to the output of the manufactured article, and, therefore, a comparison of the ratios which the various materials used bear to the output over several periods, forms a good test of the accuracy of the amounts charged. Any undue decrease may be attributable to reduced prices, to the omission of invoices for materials purchased, or to errors in the stock. Similarly, large increases may be caused by increased prices, the inclusion of invoices of goods not received or taken into stock, or to errors in the stock itself. (See also COST ACCOUNTS, p. 349.)

MEDICAL PRACTITIONERS, AUDITORS AND.

(See AUDITING, p. 115.)

MEETINGS OF CREDITORS IN BANKRUPTCY.

(See BANKRUPTCY, MEETINGS OF CREDITORS IN.)

MEETINGS OF LIMITED COMPANIES.

A company limited by shares is required to hold—

- (a) A statutory meeting;
- (b) An annual general meeting;
- (c) Extraordinary general meetings, if such be necessary.

The first meeting is usually the statutory meeting, but as this is dealt with in a separate article (p. 885), no further reference need be made here.

ANNUAL GENERAL MEETING.—Section 64 of the Companies (Consolidation) Act provides that a general meeting of every company shall be held once at least in every calendar year, and not more than fifteen months after the holding of the last preceding meeting. A fine not exceeding £50 is the penalty for default, and every director, manager, secretary, and every officer of the company who is knowingly a party to the default is liable. Moreover, if the meeting is not held in accordance with this section, the Court may, on the application of any member of the company, call

or direct the calling of a general meeting of the company. It sometimes happens that the accounts are not ready by the time the meeting should be held. In this case, the proper procedure is to hold the meeting, transact routine business, and then adjourn the meeting. Provisions for the calling of the annual general meeting are usually found in the Articles of Association, but subject to anything therein contained: (a) a meeting may be called by seven days' notice in writing, served on every member in the manner in which notices are required to be served by Table A; (b) five members may call a meeting; (c) any person elected by the members at the meeting may be chairman; (d) every member shall have one vote.

The regulations contained in Table A with regard to the notice of meetings are: (a) notice may be given personally, or through the post; (b) service of notice is deemed to have been effected if a letter properly stamped and addressed and containing the notice has been posted; (c) joint holders are notified if the first joint holder is notified.

It is important that the notice of the meeting be authorised by the directors, and be served strictly in accordance with the regulations; for, if proper notice is not given, any resolutions passed at the meeting are invalid, unless the Articles provide for this contingency, which is usually the case.

Only members of the company are entitled to attend, and when proxies are allowed the Articles usually require that the proxy shall also be a member, except where a company is a member of another company, in which case Section 68 provides that any authorised person may attend as representative. Every member is entitled to notice unless, by the Articles, certain members are excluded. For instance, the Articles of some companies stipulate that preference shareholders shall not be entitled to notice, and, of course, debenture holders, not being members, are not entitled. Similarly, the executors or administrators of a deceased member are not entitled to notice until registered as members, unless the Articles make provision therefor.

The business of a general meeting consists of ordinary business and special business. Ordinary business is usually specified in the Articles as passing accounts, sanctioning dividends, receiving reports, electing officers. Other business is usually regarded as special, and of this, notice of its general nature must be given.

The annual return and summary required by Section 26 of the 1908 Act must be made up on the fourteenth day after the first or annual general meeting in the year, and completed within seven days after the date to which it has been made up.

EXTRAORDINARY GENERAL MEETING.—It is often necessary for a company to transact

business which does not fall within the category of ordinary routine business, and in such a case an extraordinary meeting may be held at which only the special business for which it has been convened may be transacted. The directors are empowered to call an extraordinary general meeting whenever they think it necessary, but apart from this, the shareholders have a statutory right to convene an extraordinary meeting in certain circumstances. This statutory right is given by Section 66 of the 1908 Act, which states that—

(1) Notwithstanding anything in the Articles of a company, the directors of a company shall, on the requisition of the holders of not less than one-tenth of the issued share capital of the company upon which all calls or other sums then due have been paid, forthwith proceed to convene an extraordinary general meeting of the company.

(2) The requisition must state the objects of the meeting, and must be signed by the requisitionists and deposited at the registered office of the company, and may consist of several documents in like form, each signed by one or more requisitionists.

(3) If the directors do not proceed to cause a meeting to be held within twenty-one days from the date of the requisition being so deposited, the requisitionists, or a majority of them in value, may themselves convene the meeting, but any meeting so convened shall not be held after three months from the date of the deposit.

(4) If at any such meeting a resolution requiring confirmation at another meeting is passed, the directors shall forthwith convene a further extraordinary general meeting for the purpose of considering the resolution and, if thought fit, of confirming it as a special resolution; and, if the directors do not convene the meeting within seven days from the date of the passing of the first resolution, the requisitionists, or a majority of them in value, may themselves convene the meeting.

(5) Any meeting convened under this section by the requisitionists shall be convened in the same manner, as nearly as possible, as that in which meetings are to be convened by directors.

MEMBERS, REGISTER OF.

By Section 25 of the Companies (Consolidation) Act every company is required to keep a register of its members in one or more books. The register must contain the following particulars—

Name, address and occupation of each member; the number of shares held, and their distinctive numbers; the amount paid or agreed to be paid on the shares; the date on which each person was entered on the Register; the date on which any person ceased to be a member. Other particulars may be entered if desired, but the above are the

FORM OF REGISTER OF MEMBERS

Date of Entry as a Member
Date when Ceased to be a Member

Folio in Share Ledger.	NAME.	ADDRESS.	Occupation or Title.	No. of Shares.	Amount paid on each Share.

SHARES REGISTERED AND PURCHASED						SHARES SOLD AND TRANSFERRED.						Balance of Shares held.	
Date of Registration.	Transfer No.	Folio of Trans- feror.	Cer- tificate No.	Distinctive Nos. of Shares, both Nos. inclusive.		Date of Registration.	Transfer No.	Folio of Trans- feree.	Cer- tificate No.	No. of Shares.	Distinctive Nos. of Shares, both Nos. inclusive.		
				From	To						From		To

statutory requirements. The register must commence from the date of the registration of the company, but as in some cases this is impracticable, the application and allotment sheets usually constitute the register until such time as the latter is written up. As the subscribers to the Memorandum are deemed to become members of the company at the date of its incorporation, their names should be entered first on the register, the date of the incorporation of the company being inserted as the date on which they became members. In the case of other shareholders, the date on which the entry is actually made in the register should be entered. By Section 27 no notice of any trust, expressed or implied or constructive, shall be entered on the register or be receivable by the Registrar. This applies only to companies registered in England or Ireland; it does not apply to companies registered in Scotland. An exception to this rule is made in the case of shares held by the Public Trustee. Section 30 requires that the register of members be kept at the registered office of the company, and, except when closed as provided by Section 31, shall be open to inspection for not less than two hours a day. Any member may inspect the register without payment, but any other person may be charged a fee not exceeding 1s. for each inspection. Heavy penalties are imposed for refusal to allow inspection. Although the right to inspect the register does not give the right to take copies, the Act provides that any member or other person may require a copy of the register or any part thereof on payment of 6d. (or less if the company so prescribes) for every 100 words. When this is done it is usual to count each figure as one word.

The register may be closed in pursuance of Section 31 for a period not exceeding 30 days in each year, and during the time the register is closed there is no right of inspection. Notice of the closing must be given by advertisement in some newspaper circulating in the district where the registered office is situated.

If the name of any person is, without sufficient cause entered in, or omitted from the register, or if default is made or unnecessary delay takes place, in entering the fact that the person has ceased to be a member, application may be made to the Court by the person aggrieved, or any member, or the company, for rectification of the register. The annual list and summary must be contained in a separate part of the register as provided by Section 26 (4).

COLONIAL REGISTER.—If a company carries on business in a Colony, it may, if authorised by its Articles, keep a register of members resident in the Colony. If such Colonial register is kept, notice of the situation of the Colonial office must be given to the Registrar, who must also be notified

if the register is discontinued. It is also provided that shares registered in the Colonial register must be distinguished from the shares registered in the principal register. By Section 35 a Colonial register is deemed to be part of the company's register of members, and must be kept in the same manner. Entries made in the Colonial register are transmitted from time to time, and entered at the head office in a duplicate of the Colonial register. The object of keeping this register is to avoid the delay which would occur if reference had to be made to the head office before a transfer could take place.

The rulings on pp. 700 and 701 show two forms of register of members. It will be noticed that in the second is kept the share account of each shareholder. The book thus becomes not only a register of members, but also a share ledger.

MEMORANDUM OF ASSOCIATION.

This is the document in which are defined the powers of an incorporated company. The activities of the company are confined to the limits set forth in the Memorandum and anything done outside these limits is *ultra vires*. Section 3 of the Companies (Consolidation) Act, 1908, states that the Memorandum of Association of a company limited by shares must contain (a) the name of the proposed company, with the word "limited" as the last word in the name; (b) the situation of the registered office; (c) the objects for which the proposed company is being formed; (d) a statement that the liability of the members is limited; (e) the amount of capital with which it is to be registered, and the number and amount of the shares into which it is to be divided. If the company is limited by guarantee, and has a share capital, the Memorandum must contain the above clauses, with an additional one stating that each member undertakes to contribute an agreed sum in the event of the company being wound up. This liability would be in addition to that represented by amounts outstanding on the shares. If a company limited by guarantee is registered without share capital, the clauses would be as just indicated, with the omission of that referring to the capital. The Memorandum of an unlimited company must state the name of the company, the location of the registered office, and the objects of the company. It may be useful to deal with some of the above points a little more fully.

NAME.—With regard to the name of the company the word "limited" must be the last word in such name, unless the company is being formed for promoting commerce, art, science, religion, charity, or other useful object, and intends to apply its profits or other income in promoting its objects, and to prohibit the payment of any

dividend to its members, in which case the company may, by obtaining a licence from the Board of Trade, be registered without the word "limited." Section 8 provides that a company may not be registered with a name already on the register, or so nearly resembling that name as to be likely to deceive. An exception is made in the case of a company which is being wound up, and which has signified its consent to the use of its name in such manner as the Registrar requires. Subject to the approval of the Board of Trade, and to the passing of a special resolution, a company may change its name. The decision of the Registrar as to the availability of a name is final, unless the applicant can show that the Registrar has used his judicial discretion wrongly. If the proposed name is one which implies that the company is under Royal patronage, such name may not be used unless the written consent of the Home Secretary is obtained. Restriction is also placed on the use of such expressions as Emperor, Crown, Imperial, etc., and the use of the word "Anzac" or any word closely resembling it is prohibited unless the authority of the Secretary of State given on the request of the Government of the Commonwealth of Australia or of the Dominion of New Zealand is given.

The name of the company must appear on the outside of every office in which trade is carried on; it must be engraved on the seal of the company, and must be mentioned in all notices, advertisements, bills of exchange, etc., issued by the company. If any director, manager, or officer of a company signs or authorises the signing of any bill of exchange or order for money or goods in which the company's name is not mentioned, such person is liable to the holder of the document if the company fails to pay it.

LOCATION OF OFFICE.—Regarding the registered office, all that is required in Clause B is a statement of the country in which such office will be situated. The precise postal address is not required, as this will be furnished in another document. In this connection it may be mentioned that Wales is included in England, so that a company whose registered office is to be in, say, Cardiff, would be registered in England. The statutory books must be kept at the registered office, and these books cannot be mortgaged, nor can a solicitor or accountant hold a lien on them for money due to him by the company. A company which is incorporated abroad, but has a place of business in this country, must file with the Registrar the name and address of some person who will accept notice on behalf of the company. This is provided for in Section 274 of the 1908 Act.

OBJECTS.—This is the most important clause and requires very carefully drafting in order that the company's activities may not be hampered through lack of power to do what it wishes to do,

for it must be remembered that the company is prohibited from devoting its money to any other purposes than those for which it is formed. The main object of the company will be its particular trade or business, but in addition to this it is usual to take powers to do many things, some of which may appear to be quite foreign to the main object. These general objects are inserted in order that the company may not fail in its main objects owing to lack of power to do certain things which are incidental to the main objects, but it should be noted that, unless it is specifically stated to the contrary, the general objects must be read in conjunction with the main objects and not apart from them. An act done outside the scope of the Memorandum is void, and is incapable of ratification even if agreed to by the whole of the members of the company.

LIABILITY.—All that is required in this clause is a statement to the effect that the liability of the members is limited.

CAPITAL.—Companies with a share capital are required to state in this clause the amount of the registered capital, and its division into shares of a fixed amount. If it is proposed that the shares shall carry different rights, this information should be stated in the Articles of Association, and the clause in the Memorandum be confined to what is legally required, viz., the amount of the share capital and the division thereof into shares of a fixed amount. The reason for this is that if the rights of the shareholders are stated definitely in the Memorandum of Association they are unalterable, unless the Memorandum of Association authorises alteration, or the capital is reorganised under Section 45, or under a scheme of compromise or arrangement under Section 120; whereas if the rights are defined in the Articles of Association they may be altered if necessary.

The Memorandum of Association requires the signatures of at least seven persons if the company is a public company, and two if a private company. These signatures must be written in the presence of at least one witness, who will attest the signatures. A duly authorised agent may sign for a subscriber. Each subscriber must state opposite his name the number of shares he agrees to take, and insert his address and occupation. In this connection it may be stated that the shares subscribed for on the Memorandum of Association may be paid for in money or in money's worth, e.g. rendering personal services. The Memorandum of Association must be stamped as if it were a deed (10s.), and must also bear capital stamp duty according to the scale set out in Schedule B to the Companies Act, 1908.

Except as expressly provided in the 1908 Act the Memorandum of Association is unalterable. The Act, however, does provide that certain alterations may be made. For instance, Section

8 (3) provides that the company's name may be changed if a special resolution is passed, and the approval of the Board of Trade in writing is obtained. Similarly, Section 9 authorises a company to alter its objects clause if the alteration enables the company to carry on its business more economically or efficiently, or by new and improved means. It may also alter this clause to enlarge or change the place of its operations, or to carry on a new business in conjunction with the old, and also if it wishes to restrict or abandon any of its objects. Again, if so authorised by the Articles, a company limited by shares may increase, consolidate, or sub-divide its share capital, convert paid up shares into stock, and *vice versa*, or cancel shares not taken up or agreed to be taken up at the date of the passing of the resolution. Another alteration which may be effected is provided by Section 81, which states that, if authorised by its Articles, a company may by special resolution alter its Memorandum so as to render unaltered the liability of its directors, manager, or any managing director. All these alterations must be carried out strictly in accordance with the requirements of the Act, to the various sections of which reference should be made.

MERCANTILE AGENT.

An agent who is concerned exclusively with mercantile matters. The principal classes of such agents are factors, brokers, auctioneers, partners, and, to a certain extent, servants.

MERGER.

This legal term means the swallowing up of some right in another, and it is generally applied to the case where the less is absorbed by the greater. Thus, if a person has a limited right in an estate, or a charge upon it, or anything similar, the gaining of the complete ownership of the estate extinguishes the rights which have existed separately, and these rights become merged in the ownership. Similarly, if two or more parties enter into a parol contract, and the terms of the contract are afterwards set out in a deed, or contract under seal, the simple contract made in the first instance becomes merged or extinguished in the specialty contract.

MESSUAGE.

This is an old French law term, which really signifies a "dwelling-house," and is connected more or less closely with "mansion" and "manse." At one time its meaning was more extensive, as it not only signified the dwelling-house but also all buildings adjoining or attached to it, together with the curtilage, gardens, and the land in which the house was built, and any pleasure grounds belonging to it.

MINERAL RIGHTS DUTY.

This is a duty imposed by the Finance (1909-10) Act, 1910, in respect of the rental value of all rights to work minerals lying under the lands of the owners thereof, and also in respect of all wayleaves. By Section 20 of the Act, it is provided, in the first subsection, that there shall be charged, levied, and paid for each financial year "on the rental value of all rights to work minerals and of all mineral wayleaves, a duty (in this Act referred to as a mineral rights duty) at the rate in each case of one shilling for every twenty shillings of that rental value," and then the section proceeds—

"(2) The rental value shall be taken to be—

(a) Where the right to work the minerals is the subject of a mining lease, the amount of rent paid by the working lessee in the last working year in respect of that right ; and

(b) Where minerals are being worked by the proprietor thereof, the amount which is determined by the Commissioners to be the sum which would have been received as rent by the proprietors in the last working year if the right to work the minerals had been leased to a working lessee for a term and at a rent and on conditions customary in the district, and the minerals had been worked to the same extent and in the same manner as they have been worked by the proprietor in that year :

Provided that the Commissioners shall cause a copy of their valuation of such rent to be served on the proprietor ; and

(c) In the case of a mineral wayleave, the amount of rent paid by the working lessee in the last working year in respect of the wayleave :

Provided that if in any special case it is shown to the Commissioners that the rent paid by a working lessee exceeds the rent customary in the district, and partly represents a return for expenditure on the part of any proprietor of the minerals which would ordinarily have been borne by the lessee, the Commissioners shall substitute as the rental value of the right to work the minerals or the mineral wayleaves, as the case may be, such rent as the Commissioners determine would have been the rent customary in the district if the expenditure had been borne by the lessee.

"(3) Every proprietor of any minerals and every person to whom any rent is paid in respect of any right to work minerals or of any mineral wayleave shall, upon notice being given to him by the Commissioners requiring him to give particulars as to the amount received by him in respect of the right or wayleave, as the case may be, and where the proprietor is working the minerals, particulars as to the minerals

worked, make a return in the form required by the notice, and within the time, not being less than thirty days, specified in the notice, and in default shall be liable to a penalty not exceeding fifty pounds to be recovered in the High Court.

"(4) Mineral rights duty shall be assessed by the Commissioners and shall be payable at any time after the first day of January in the year for which the duty is charged, and any such duty for the time being unpaid shall be recoverable as a debt due to His Majesty from the proprietor of the minerals, where the proprietor is working the minerals, and in any other case from the immediate lessor of the working lessee. As between the immediate lessor and the working lessee, the duty shall be borne by the immediate lessor, notwithstanding any contract to the contrary, whether made before or after the passing of the Act.

"(5) Mineral rights duty shall not be charged in respect of common clay, common brick clay, common brick earth, or sand, chalk, limestone, or gravel."

No reversion duty is payable upon the determination of a mining lease, and no increment duty is payable upon the granting of the same. For full particulars as to these matters, as well as to the exceptions made under certain conditions and in certain cases in the case of mining leases granted before the 30th April, 1909, the Finance Act itself must be consulted.

MINERAL ROYALTY.

(See ROYALTIES.)

MINIMUM RENT.

(See ROYALTIES.)

MINIMUM SUBSCRIPTION.

This refers to the amount, if any, fixed by the Memorandum of Association or Articles of Association of an incorporated company, and named in the prospectus, or statement in lieu of prospectus, as the minimum amount which must be subscribed before the directors will proceed to allotment. Any amount may be fixed, but if no amount is fixed then the whole of the amount of the share capital offered for subscription constitutes such minimum. The minimum subscription is important in connection with the first allotment of shares, for by Section 85 no allotment shall be made of any share capital of a company offered to the public for subscription unless the minimum subscription has been taken up, and the amount payable on application for the amount so fixed (or for the whole amount offered for subscription) has been paid to and received by the company. The amount fixed (or the whole of the capital offered) must not include shares payable otherwise than in cash.

The minimum subscription is also referred to in Section 87, which provides *inter alia* that a

public company shall not commence any business or exercise any borrowing powers unless shares held subject to the payment of the whole amount thereof in cash have been allotted to an amount not less in the whole than the minimum subscription.

MINING AND COLLIERY CONCERNS, AUDIT OF.

(See AUDITING, p. 108.)

MINUTE BOOKS, AUDITORS AND.

(See AUDITING, p. 72.)

MISDEMEANOUR.

A criminal offence which does not fall within the category of felonies. Generally, it is the name applicable to the less serious offences known to the law. But this is not always the case, as perjury is a misdemeanour, whereas simple larceny is a felony. The difference between felony and misdemeanour really belongs to the history of law, as in cases of felony a convicted person was deprived of his goods, in cases of misdemeanour he was not. In all modern statutes the offence is always stated to be either a felony or a misdemeanour. A misdemeanour is triable on indictment, inquisition, or information. There are no accessories after the fact to misdemeanours.

MISFEASANCE.

This is a legal term used in connection with the law of torts, and is generally understood to mean either the actual doing of an act which is wrongful in itself, or the doing of an act which is in itself lawful in a wrongful manner. The actual doing of a wrongful act, however, is often known as malfeasance, the word misfeasance being limited to the other action mentioned above. It is very important to distinguish malfeasance and misfeasance from nonfeasance, which signifies the mere omission to do an act, when legal liability is in question. A private individual *may be* liable for acts of omission as well as for acts of commission, that is, for malfeasance or misfeasance and nonfeasance, under certain circumstances, but it is a well established rule of law that a corporate body can only be held responsible for malfeasance or misfeasance and never for nonfeasance.

MISREPRESENTATION.

Any statement made by a party to a contract during the course of the negotiations which is inaccurate, and which is made for the purpose of inducing the other party to act upon it, and upon which the other party does, in fact, act to his detriment. If this inaccurate statement is made with a knowledge of its falsity, there is fraudulent misrepresentation, or, more simply, fraud. When a contract has been entered into and has been induced by misrepresentation, such contract is voidable at the option of the person who has been damnified.

He has, in fact, been misled and misinformed, and consequently there has not been that *consensus ad idem* which is essential to the formation of every contract. In order, however, that misrepresentation may be a ground for rescinding a contract, it must be one of fact and not of law, it must have been made by one of the parties to the contract, and the contract itself must have been induced by the other party relying and acting upon the misrepresentation.

MISTAKE.

This word, when used in an everyday sense, is easily understood, but when it is used in a legal sense, its significance is much limited. It means such a misapprehension of the facts of a certain transaction as to make it clear that the parties were never in real agreement at all, each of them having had his mind fixed upon something not contemplated by the other. Mistake is, in most cases, a good ground for avoiding a contract. But the mistake must be one of fact and not of law, since it is a well-known maxim that "ignorance of the law excuses no one"—*ignorantia juris neminem excusat*—unless the mistake of law is so egregious as to suggest imbecility, or when it is accompanied with imposition.

The mistakes of fact which are sufficient to invalidate a contract, otherwise regular upon the face of it, are the following—

(1) Mistake as to the subject matter of the contract. This may refer either to the existence of the subject matter at the time of the formation of the contract, or to its identity. Unless the parties are *ad idem*, there can be no contract.

(2) Mistake as to the parties to the contract. This arises when one of the parties intending to contract with one person makes an agreement with another. Certainty is one of the essentials of a valid contract, and a mistake of this kind renders an agreement invalid.

(3) Mistake as to the nature of the contract. The most familiar example of this species of mistake is where a blind or illiterate person is prevailed upon to sign a deed or other document, being told that it is something altogether different. The mistake, which may amount to fraud on the part of some person or other, arises from the fact that the mind of the signatory does not accompany the signature.

It is obvious that the questions arising out of mistake may be very numerous and very difficult, and the above summary is all that can be given to show the nature of the defence that may be set up in certain cases where a contract has been entered into under a complete misapprehension.

MODELS AND PATENTS.

The initial fees and costs of obtaining patent rights may be capitalised, and should be charged to Patents Account. If the patent is likely to be

a valuable one, the cost of *successful* experiments may also be added to this account. If acquired by purchase, then the purchase price and the costs of the assignment may be debited to Patents Account.

All renewal fees must be charged against revenue.

Patent rights depreciate chiefly by effluxion of time. The monopoly granted to the patentee or his successors and assignees expires fourteen years after the right is first granted. The rate of depreciation applied should, therefore, be such as will completely wipe out the book value of the patent rights within this period. This, however, is the limit of time to be allowed. In determining the rate of depreciation regard should be had to the probable time during which the patent can be *profitably* worked. In the case of untried patents, the rate of depreciation should be much heavier than that suggested above.

The auditor should require the production of the original Letters Patent and of any assignment thereof to the business. He should further require the production of all renewal receipts in order to satisfy himself that the rights have not lapsed by failure to pay the necessary fees.

The intrinsic value of models constructed for patenting purposes is usually small, and, as any value of an exceptional nature attaching to them through their connection with the patents may be deemed to be included in the value of the patent rights, it is advisable that their cost should be provided out of the revenue of the period within which it is incurred.

In cases where, however, considerable expenditure has been incurred upon models, the expenditure may, if the patent is successful, be temporarily capitalised, and written off over a short term of years.

MONOPOLY.

The sole right of sale and supply of an article. This word is mainly of importance in economic questions.

MONTH.

The primary meaning of the word "month" in legal documents is "lunar month," and unless it is so provided by statute, as it is in the Bills of Exchange Act, 1882, and the Sale of Goods Act, 1893, the meaning "calendar month" is not generally applicable even in commercial documents. It can only bear that meaning in cases where, according to the ordinary rules of construction of documents, a secondary meaning can be admitted. This point was made quite clear in the case of *Bruner v. Moore*, 1904, 1 Ch. 305.

MORTGAGE.

Put in its condensed form, a mortgage is a charge which a borrower gives to a lender upon a part or the whole of his property. Stated in

legal language, it is a conveyance or disposition of real or personal property by a borrower, called the mortgagor, in favour of a lender, called the mortgagee, by way of security for the repayment of money borrowed, together with interest. The word mortgage is now almost invariably confined to transactions of this character in connection with land; when personal property (excluding leaseholds) is the security for money lent, the mortgage is known as a bill of sale (*q.v.*).

When there is a mortgage of freeholds, the fee in the land is conveyed by the mortgagor to the mortgagee, subject to an agreement for the repayment of the money lent on a fixed day, usually six months from the date of the advance, together with interest. The mortgagor generally remains in possession. At common law, if the borrower failed to repay the loan on the due date, the lender was entitled to eject him; but equity, looking at the true nature of the transaction established the maxim "once a mortgage, always a mortgage," and now a mortgagor has always an equity of redemption, that is, the right to get back his property, upon payment of what is due together with interest and costs, at any time before his right has been absolutely foreclosed by an order of the Court.

Leasehold property may also be mortgaged, either by assignment or by under-lease. The latter method, however, is to be preferred to the former. Copyholds may be mortgaged. A mortgage of this kind of property is effected by a conditional surrender to the mortgagee being entered on the rolls of the manor, making such conditional surrender void on the payment of the loan with interest.

The rights of the parties to a mortgage have been gradually formulated by the Court of Chancery and by Statute and may be thus summarised.

The following are the rights of the mortgagee—

(1) He has the right as of course to sue for his money at any time after it has become due. As is well known, however, a mortgage is looked upon as an investment over a considerable period, and, although the date of repayment of the loan is generally fixed at the expiration of six months after the mortgage is made, the mortgagee rarely presses for repayment until he is really in want of his money.

(2) If the mortgagor makes default in payment after three months' notice has been given to him by the mortgagee, or if interest has become in arrear for two months, or if there has been any breach by the mortgagor of the covenants contained in the mortgage deed other than the covenant for the payment of the mortgage money or interest on the fixed day, the mortgagee may enter into possession of the mortgaged property, or he may bring an action for foreclosure (*q.v.*), or he may appoint a receiver, or he may sue the

mortgagor for principal and interest. If proceedings are taken for foreclosure and the mortgagor fails to comply with the order made by the Court on the same, the mortgagee takes possession and the mortgagor is shut out for ever.

(3) The mortgagee has a power at any time to insure and to keep insured any buildings on the mortgaged property, and he is entitled to add the premiums paid to the amount of his security.

(4) In most cases, unless expressly excluded, the mortgagee in possession, if he takes possession without any action of foreclosure, has the right to sell the property when the mortgagor is in default. By exercising his power of sale the mortgagee does not take the property in lieu of the debt so as to extinguish it, as he does by foreclosure, but he can sue the mortgagor for any deficiency in the money arising from the sale to meet the principal, interest, and costs of the mortgage debt. On the other hand, he must, of course, pay to the mortgagor any surplus, if the sale realises more than enough to pay the principal, interest, and costs.

The following are the principal rights of the mortgagor—

(1) The mortgagor must give six months' notice if he wishes to pay off the loan, or pay interest for that time. This was always the rule in equity, and it has not been changed so far as the mortgagor is concerned, though the length of notice to be given by the mortgagee, if he wishes to call in his money, has been fixed at three months, as above mentioned.

(2) He can at any time after giving such notice, or when the mortgagee is pursuing any of his remedies, tender the principal, interest, and costs to the mortgagee, and if the latter refuses to accept such tender, institute an action for redemption.

(3) He can, even when the mortgagee has taken possession, demand an account of all rents and profits received by the mortgagee.

(4) He may at any time inspect his title deeds which are in the hands of the mortgagee.

(5) He has a statutory power, so long as he is in possession, except in so far as a contrary intention is expressed in the mortgage deed, to make leases and contracts of tenancy of any parts of the mortgaged property—agricultural and occupation tenancies not to exceed twenty-one years, and building leases not to exceed ninety-nine years. Such leases and tenancies must take effect in possession not more than twelve months after date, and must reserve the best rent that can reasonably be obtained. They must also contain a covenant by the tenant to pay the rent, and a counterpart must be executed by the tenant.

(6) On the discharge of the mortgage moneys, the mortgagor has a right to demand his property back in its integrity. In other words, on redemption, he is entitled to have back that which he

hypothecated unfettered, and anything which would prevent his getting it back when his obligation is fulfilled will not be permitted. In technical language, nothing will be allowed which will "clog the equity of redemption." For example, in a mortgage deed by a publican to brewers, a covenant by the borrower *after discharge* of the mortgage to sell beer bought of the lenders only, is bad, and cannot be upheld, inasmuch as the "tie" would reserve to the lender a hold on the property after redemption and make it less valuable than when it was mortgaged.

By statutory enactments the time during which a mortgagee has the right of exercising his power of foreclosure, is limited to twelve years from the date when the right first accrued, or to twelve years from the time of the last payment of any part of the principal money or interest of the mortgage debt. Also if the mortgagee is in possession, the mortgagor is confined to the same limits of time for exercising his right to redeem.

It has been stated above that the principal is generally made repayable six months after the date of the mortgage deed. The parties are not bound, however, by these limits. They may choose their own times. But there must be a stipulation as to repayment at some time. No mortgage can be made irredeemable.

The mortgages referred to in the present article have been those which are evidenced by deeds. These are known as "legal mortgages." When mortgages are made by the mere deposit of title deeds (though these are often accompanied by a memorandum of deposit) they are known as "equitable mortgages." The only proper legal remedy of the mortgagee in the case of an equitable mortgage is that of foreclosure. (See EQUITABLE MORTGAGE.)

MORTGAGE LOAN AND DEPOSIT ACCOUNTS.

A few points of varying importance and interest in relation to transactions of the description indicated by the title, which consist of fixed loans on mortgage or security of such subjects as land, buildings, works, and rates, the principal of which is either redeemable in full on a fixed date or by periodical instalments combining both principal and interest over a given period, the latter being the usual mode of repayment or redemption.

Our observations herein will apply in the main to companies rather than to building and similar societies, the latter being conducted according to the Building Societies Acts. Many of our notes, however, are not inapplicable to building and other societies.

The auditor, in the first instance, will make himself acquainted with the constitution and objects of the undertaking, its Memorandum and Articles of Association, or its rules and regulations, and see that the transactions are not beyond or in

contravention of its authorised powers. As regards the mortgage deeds, these he will inspect in the usual way in conjunction with the Register of Mortgages, noting any prescriptions as to proportions of class of mortgage and of amount. He will, of course, peruse carefully the minutes of the Board for the authority of the advances on mortgages, which will also contain particulars from time to time of deposits received and uplifted or withdrawn, terms, and other conditions. Where varying sums are so advanced, and particularly for varying periods and at different rates, it will be generally found that a table for each transaction has been prepared, of which the following is an example. In such circumstances the full table relating to each loan should be entered in a book—Mortgage Loans Book—and suitably indexed.

JOHN JONES

Loan of £5,000 made on-----
repayable with interest at the rate of 6 per cent.
per annum by four half-yearly instalments of £-----
combining both principal and interest on the
-----and the-----in
each year over a period of four years.

First Instalment Due-----
Final Instalment Due-----
Board Minute-----

TABLE.

Amount of Principal of Loan out- standing at the beginning of each period.	Interest thereon at the rate of 6% per annum.	Instalment Payable.		Amount of Principal of Loan out- standing at end of each period.
		Date.	Amount.	
£ 5000 3804·86467 2573·87528 1305·95620	£ 150. 114·14594 77·21625 39·17868		£ 1345·13533 1345·13533 1345·13533 1345·13533	£ 3804·86467 2573·87528 1305·95620 —
Total . .	380·54087		5380·54132	—

Here the calculation is—

$$\begin{aligned}
 & \frac{5,000}{\left(1 - \frac{1}{(1.03)^4}\right)} = \frac{5,000}{\left(1 - \frac{1}{1.1255088}\right)} \\
 & \quad \frac{5,000}{.03} = \frac{5,000}{.03} \\
 & \quad = \frac{5,000}{\left(\frac{1 - .888487055}{.03}\right)} = \frac{5,000}{.111512945} \\
 & \quad = \frac{5,000}{.03} = £1,345.13533, \\
 & \quad 3.7170981
 \end{aligned}$$

the half-yearly instalment.

The Cash Book, it may be stated, may be here conveniently and usefully designed on the lines of that on the next page.

CASH BOOK

Dr. SIDE.

Cr. SIDE.

[illegible]

BORROWER'S LEDGER

J. JONES

LOAN of £5,000 on 1st January, 19... as per Board Minute dated 26th December, 19..., at the rate of 6 per cent. per annum, payable by four half-yearly instalments of £1345·1353, combining both principal and interest on the 30th June and the 31st December, in each year, over a period of two years.

The first instalment payable_

The final instalment payable

Insurance Record.

Mortgage Record

Date.	Particulars.	F.	Amount of Instalment.		Interest on Arrears.	Insur- ance.	Other Charges.	Amounts.
			Principal.	Interest.				
Jan. 1	To Cash . . .		£	£				£
June 30	" Instalment due		1195'13533	150				1345'13533
Dec. 31	" "		1230'98939	114'14594				1345'13533
Jan. 1	To "							
June 30	" "		1267'91908	77'21625				1345'13533
Dec. 31	" "		1305'95665	39'17868				1345'13533

a single group) in the Balance Sheet, especially in the case of discount companies and others who pursue a deposit business.

With regard to building societies, the auditor must make himself familiar with the Building Societies Acts, 1874 and 1894, and the particular society's rules and tables. With regard to borrowing, in a permanent society the total amount received on deposit or loan and not repaid by the society is not at any time to exceed two-thirds of the amount for the time being secured to the society by mortgages from its members.

MORTGAGE OF A SHIP.

When a British ship is mortgaged, the mortgage must be in the form set out in the Merchant Shipping Act, 1894. The document must be produced to the registrar of shipping at the ship's port of registry and duly recorded there. If there are several mortgages, priority depends upon the date of registration, and not upon the date of the execution of the mortgage debt.

MORTGAGES.

(See AUDITING, pp. 87, 94, 96; BALANCE SHEET, p. 145; MORTGAGE.)

MORTGAGES AND CHARGES, REGISTRATION OF.

Under the Companies (Consolidation) Act, 1908, a double system of registration of mortgages and charges is set up. The operative sections setting out the requirements relating to registration are Sections 93 and 100. Section 93 makes provision for the registration at Somerset House, whilst Section 100 provides for the keeping by the company of a register of mortgages specifically affecting the property of the company. The duty of attending to the work of registration falls primarily upon the secretary and directors of the company. The auditor, however, has some responsibility in relation to these matters. Under Section 65 of the Companies Act, it is necessary for the auditor to certify as to the correctness of receipts and payments of the company as shown in the statutory report. It necessarily follows, therefore, that where debentures have been issued and money received on account of debentures it is incumbent upon the auditors to see, as they have a right, the register of debentures and also the register of mortgages and charges. This register should always be at the disposal of the auditor, who, whilst he is not concerned with the registration as such, may rely upon the entries in the register for details of mortgages and charges appearing in the books of the company. (See Form on p. 712.)

COMPANY'S REGISTER.—A company's register must contain full particulars of all the debts due from the company to persons holding security. Section 100 requires that—

(1) Every limited company shall keep a

register of mortgages and enter therein all mortgages and charges specifically affecting property of the company, giving in each case a short description of the property mortgaged or charged, the amount of the mortgage or charge, and (except in the case of securities to bearer) the names of the mortgagees or persons entitled thereto.

(2) If any director, manager, or other officer of the company knowingly and wilfully authorises or permits the omission of any entry required to be made in pursuance of this section, he shall be liable to a fine not exceeding £50.

Registration under this section is not absolutely essential from the point of view of the person entitled to the mortgage or charge. The charge remains valid notwithstanding failure on the part of the company's officers to keep the register. The register of mortgages and charges is open for inspection to all creditors and shareholders free of charge, and to other persons on payment of an inspection fee, not exceeding one shilling, as may be fixed by the company. No right to receive copies of the register is provided in the Act, and it is deduced that the right to inspect includes the right to take copies (*Nelson v. Anglo-American Company*, 1897, 1 Ch. 130). It should be remembered that copies of the register of members may not be taken by persons inspecting, as provision is made for copies to be supplied on payment of a fee.

The register above mentioned is not the register of debentures generally kept by a limited liability company; this register is not a statutory book, but is similar to the register of shareholders. Like the register of mortgages and charges the register of debenture holders is open for inspection, but only to debenture holders and shareholders in the company. A copy of the trust deed for securing an issue of debentures is also obtainable by a debenture holder or shareholder on payment of a fee not exceeding one shilling in the case of a printed deed, and in the case of a trust deed, not in print, a fee of sixpence for every hundred words may be charged. The register of debenture holders may be closed in accordance with the terms of the Articles for a period not exceeding thirty days, thus bringing this register into a line with the other books of the company.

REGISTRATION WITH THE REGISTRAR.—In addition to the registration described in the foregoing section, a more public form of registration is necessary under the terms of Section 93 of the Companies (Consolidation) Act, 1908. This section lays down that every mortgage or charge created by a company after the 1st July, 1908, either—

1. A mortgage or charge for the purpose of securing any issue of debentures; or

2. A mortgage or charge on uncalled share capital of the company; or

3. A mortgage or charge created or evidenced by an instrument which, if executed by an individual, would require registration as a bill of sale ; or

4. A mortgage or charge on any land, wherever situate, or any interest there ; or

5. A mortgage or charge on any book debts of the company ; or

6. A floating charge on the undertaking or property of the company ;

shall, so far as any security in the company's property or undertaking is thereby conferred, be void against the liquidator and any creditor of the company, unless the prescribed particulars of the mortgage or charge together with the instrument (if any) by which the charge is created are delivered to and received by the Registrar of Companies for registration within twenty-one days after the date of its creation. Failure to register does not, however, destroy the right of the person holding the mortgage or charge to receive the money due to him ; but it does have the effect of taking away his security. The registration above mentioned is popularly spoken of as the registration of debentures, but it will be noted that the registration is really that of particulars of the mortgage or charge securing the debenture or securing a loan in some other form. Thus, although no debenture may be issued, a mortgage of any of the classes of property mentioned above would require registration under the section. Registration is in reality public notice of the facts of a loan and of the security given. Previous to 1900 no formal registration was necessary, but the Companies Act of that year made provision that certain charges should, for the future, be registered. The Act, however, was not retrospective, and mortgages and charges may exist (provided they were created prior to 1900) which are not registered. If such mortgages or charges specifically affect any of the property of the company, as, for example, a mortgage or charge upon land, they will be registered in the company's own register of mortgages and charges and be returned in the total amount of all mortgages and charges required to be shown in the annual summary under Section 26 of the Companies (Consolidation) Act, 1908.

PARTICULARS TO BE REGISTERED.—The Registrar of Companies keeps a register in respect of each company showing the date of the creation of each mortgage or charge created after the 1st July, 1908, the amount secured by it, short particulars of the property concerned, and the names of the mortgagees or persons entitled to the charge. Where the charge is given for the securing of a series of debentures it is necessary to deliver to the Registrar within twenty-one days after the execution of the deed creating the charge, or if there is no such deed, after the execution of the first debenture of the series, the following particulars—

1. The total amount secured by the whole series, not the particular issue alone ; and

2. The dates of the resolution authorising the issue of the series, and the date of the covering deed by which the security is created ; and

3. A general description of the property charged ; and

4. The names of the trustees for debenture holders ; together with the deed containing the charge, or if there is no such deed, one of the debentures of the series.

The Registrar enters these particulars in the register, and where the charge is sufficient to cover more than one issue, particulars of the date and amount of each issue must be filed with the Registrar. If, however, particulars of the total amount secured have already been registered, failure to register the date and amount of an issue comprised in the total amount will not affect the validity of the debentures.

Where debentures are not debentures in a series the Registrar may not register after the lapse of twenty-one days from the creation of the charge securing the debentures, and the charge is deemed to be created at the time of the execution of the trust deed. In the absence of the trust deed the debenture itself will often be evidence of the charge, and the charge is deemed to be created when the debenture is sealed and issued.

Registration may take place even after the lapse of twenty-one days, but it will then be necessary to apply to the Chancery Division for permission to register. A Judge of this division of the High Court on being satisfied that the

REGISTER OF MORTGAGES AND CHARGES

No. of Entry	Date of Charge or of Resolution creating the Debentures.	Particulars of Property Charged.	Amount of Charge.	Names of Mortgagees or Trustees for Debenture Holders.	Date of filing the particulars with Registrar.	Date of Discharge.

omission was accidental or due to inadvertence, or that it was not of such a nature as to prejudice either shareholders or creditors, would grant relief on the application of the company or parties interested on terms that seem just and expedient, but without prejudice to any security that has been given by the company in the meantime. An ordinary unsecured creditor is not entitled to any priority where late registration is permitted.

From the point of view of an auditor of a limited liability company issuing debentures, registration can have very little effect, as the auditor would have nothing to do with the matter, and it would be no part of his business to report to the shareholders on this subject. Where, however, the client of an auditor holds debentures in a company or has advanced money to a company on security of the company's property, it will be the auditor's duty to see that the security is sufficient. As has been indicated, the holder of a mortgage or charge on a company's property loses his security if the company fails to register. It is the holder's business, therefore, to see that the charge is properly registered, and the auditor, at any rate, should advise his client on this matter, although he could not be held responsible for failing to make inquiries provided the debenture or other instrument securing the charge is on the face of it in good order. The auditor is not expected to act as a kind of amateur detective, but, nevertheless, this is a practical point worthy of attention.

REGISTRATION FEES.—On the registration of debentures fees are payable to the Registrar according to the following scale—

	£	s.	d.
Where the amount of the mortgage is £200 or under	10	0	0
Where the amount of the mortgage exceeds £200	1	0	0
Where a series of debentures is issued—			
If the total issue does not exceed £200	10	0	0
If " " exceeds £200	1	0	0
On "registration" of each successive debenture after the first	0	6	
If more than one issue in the same series—			
Registration of date and amount of each issue	5	0	
Entry of memorandum of satisfaction	5	0	

The fees payable on registration do not exempt the document creating the mortgage or charge from the ordinary duties payable in respect of such securities.

DISCLOSURES OTHER THAN REGISTRATION.

—Section 93, in addition to requiring registration of debentures, requires that disclosure shall be made of all commission or allowances made in respect of debentures or debenture stock. In the case of a public company disclosure of such allowances must be made in the prospectus or statement in lieu of prospectus issued on the formation of the company, or at any time within the two years following the allowance of such commission. A private company on conversion to a public company must disclose in its statement

in lieu of prospectus commissions or allowances made at any time in its history. All companies under the Companies Acts must in the particulars registered state the amount and rate per cent. of any commission. It is also necessary to show in the annual summary the total amount of sums paid by way of commission, and the balance sheet must show the amount paid by way of commission or any balance of such amount not written off until the whole amount has been written off.

From the auditor's point of view the above matters are of greater importance than actual registration, and he should pay attention to these requirements, as it is part of his business to see that they are complied with. Where auditing for a firm or other client holding debentures in a limited company, the auditor finds that registration has not been effected, he should remember that the holder may in such case apply for registration, recovering the expenses of registration from the company.

MOVABLE PROPERTY.

One of the divisions of property is into movable and immovable. The latter is property which is entirely connected with land, whatever the interest of the holder in the same may be, and the former embraces all those tangible things which can be moved, such as animals, money, stock in trade, and, in general terms, goods. It also includes *choses in action*. Just as immovable property does not coincide in meaning with real property, so movable property is not the same thing as personal property, though, roughly speaking, it may be said to be personal property minus chattels real. The division has no particular value in English law, but it is fraught with important consequences in international law. (See IMMOVABLE PROPERTY.)

MULTIPLE COSTS.

(See COST ACCOUNTS, p. 346.)

MUTUAL DEALINGS.

When two persons conduct their business or other transactions in such a manner that they are at times the creditor or the debtor of each other, they are said to have mutual dealings. If the dealings are numerous, a balance is struck at certain fixed periods and the difference due by the one or the other is the amount which must be paid over in satisfaction of the whole. The matter becomes of importance if one of the two becomes bankrupt and there are outstanding accounts, for the heavier debtor is allowed to set off a portion of the debt which is owed by him against that which is owed to him, and the trustee in bankruptcy can only claim the difference. Thus, suppose A, a bankrupt, owes B £150, and B, in the course of mutual dealings, owes A £200. B can set off the

£150 against his own debt, and the trustee in bankruptcy can claim no more than £50. On the other hand suppose B's debt to A is £100. B again sets off the £100 against the £150, and he can put in his proof for the balance of £50 and receive whatever dividend is paid on that amount. This is obviously the only fair way of dealing, for if B had first of all to pay the £100, the amount of his debt, and then claim a dividend on £150, he might be a heavy loser, especially if the dividend was only very small, say 1s. in the pound. In order that this mutual set-off may be allowed in the case of mutual dealings, the transactions must have taken place without any notice of an act of bankruptcy (*q.v.*) having been committed. The principle above enunciated applies to all demands provable in bankruptcy, and it includes not only trade debts, but claims for damages, liquidated

or unliquidated, provided they arise out of contract. But the debts must exist between the same parties, and must be due in the same right. From a consideration of this principle of set-off in mutual dealings, it is obvious that a party may enjoy many of the advantages of a secured creditor.

MUTUALITY.

In every simple contract there must exist an interchange of some kind between the parties, that is, if one of the parties undertakes to do something, the other must do something in return. This is the basis of consideration (*q.v.*), and the interchange is known as mutuality, which is, therefore, one of the three essentials of a simple contract, the other two being certainty as to the terms of the parties, and the *consensus ad idem*.

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NAME BOOK.

(SEE FINANCIAL HOUSES AND INVESTORS, ACCOUNTS FOR, p. 483.)

NAME OF COMPANY.

(See MEMORANDUM OF ASSOCIATION.)

NARRATION.

In accountancy, this term means the explanation of the transaction placed immediately below an entry in the Journal.

The narrations should be made as concisely as possible, and yet in words the meaning of which cannot be mistaken. Thus, should the entry have to be followed by any person unacquainted with the transaction, he is placed in full possession of the facts without having to refer either to the documents from which the entry has been made or to the person responsible for making it.

The following examples of Journal entries will instance the kind of transactions which usually require explanation by means of narrations, and may be taken as being typical of the manner in which such narrations should be made—

In the case of a Bad Debt :

F. Richards, who owes £78, is gazetted a bankrupt, paying a dividend of 8s. 3d. in the £.

	£	s.	d.	£	s.	d.
Cash	Dr.	32	3	6		
To Trustee in Bankruptcy of F. Richards	Cr.		32	3	6	
Being first and final Dividend of 8s. 3d. in the £ on £78.						
Bad Debts Account	Dr.	45	16	6		
To F. Richards	Cr.		45	16	6	
Being balance transferred to Bad Debts Account.						

In the case of Acceptance of a Bill of Exchange :

P. Boland accepted a Bill, dated 28th July, at 3 months' date, for £48 10s., less a discount of 12½% allowed him.

	£	s.	d.	£	s.	d.
Bills Receivable	Dr.	42	8	9		
Discounts Account	Dr.	6	1	3		
To P. Boland	Cr.		48	10	0	
Bill No. 29 at 3 months' date due 31st October.						

In the case of Realisation of old Machinery :

Sold for Cash, £50, an old Machine, which stands in the Private Ledger at £165.

	£	s.	d.	£	s.	d.
Cash	Dr.	50	0	0		
Profit and Loss Account (loss on realisation)	Dr.	115	0	0		
To Machinery and Plant	Cr.		165	0	0	
Old Machine sold this day.						

Writing off Depreciation :

Depreciation on Office Furniture, 5% on £1,010.							
	£	s.	d.	£	s.	d.	
Profit and Loss Account	Dr.	50	10	0			
To Office Furniture	Cr.				50	10	0
Depreciation at the rate of 5% on £1,010 for the year ended this day.							

Adjustment of Expenses on Balancing :

Rates and Taxes accrued to date,	£10	13s.	4d.			
	£	s.	d.	£	s.	d.
Rates and Taxes	Dr.	10	13	4		
To Rates and Taxes—New						
Account	Cr.				10	13 4
Amount accrued to date.						

NECESSARIES.

This term frequently arises in the cases of contracts entered into by persons whose legal capacity is subject to certain limitations, though it is one that cannot be satisfactorily defined for all cases. As regards an infant (*q.v.*), necessities for him, for which he is personally liable in contract, will include all those things which can fairly be considered reasonable in his position in life, and of which he actually stands in need at the time of their sale and delivery to him. As Coke says, "They include necessary meat, drink, apparel, physic, and such other necessities, and likewise for his good teaching or instruction, whereby he may profit himself afterwards." This opens up a very wide field, and the decided cases run very close and are sometimes scarcely distinguishable. In an action against an infant for goods sold and delivered—for this is the only way in which he can have judgment pronounced against him, seeing that he is never responsible upon an instrument, such as a bill of exchange, even though given for necessities—it is for the judge to say whether the goods supplied can be necessities under any circumstances, and then for the jury, if there is a jury, to say whether they are necessities in the special circumstances. An excessive supply of the most essential things can never be considered as necessities. Thus, an infant may purchase and be liable to pay for one or two suits of clothes, but in no case would he be liable for an order given for twenty suits. As regards a married woman, the question of necessities arises when she is living apart from her husband, without any fault of her own, and her husband fails to provide such things as are necessary for her maintenance. For such things the wife is, *primâ facie*, permitted to pledge her husband's credit. In the same manner the captain of a ship can pledge the owner's

credit, in the absence of any possibility of direct communication, for such things as are requisite for the prosecution of the ship's voyage. Lastly, a drunken person is liable for necessities supplied to him whilst in an intoxicated condition, provided the price is fair and there is an absence of unjust dealing.

NEGOTIABLE INSTRUMENTS.

These are certain documents and chattels which are entirely the creation of the law merchant, and which possess this peculiar character, namely, that the property in the documents and chattels is acquired by transfer only, provided that the whole transaction connected with the transfer is absolutely *bonâ fide*. As is well known, in the case of other documents or chattels, the transferor cannot confer a greater title to the same than that which he himself possesses, the legal maxim being *nemo dat quod non habet*.

A great authority has summed up the special characteristics of negotiable instruments as follows—

1. The property in them, and not merely the possession, passes by delivery.

2. The holder in due course of such documents is not in any way affected by any defect of title on the part of the transferor or previous holder. He holds them "free from all the equities."

3. The holder in due course can sue upon them in his own name.

Coin of the realm is practically the only chattel, apart from documents, which comes within the category of negotiable instruments. The most familiar documents of this character are cheques, bills of exchange, promissory notes, and bank notes. Other examples are Treasury bills, foreign bonds, share warrants, and share certificates to bearer. Debentures payable to bearer have now been added to the list of negotiable instruments recognised by the English courts. At one time it was thought that the list of the negotiable instruments which would be recognised was complete; but some decisions seem to point to the fact that if a clear case of custom or usage is made out that other documents, not formerly included, are in practice recognised by merchants and traders as negotiable instruments, the English

Courts will act upon the evidence of such custom and usage and admit their negotiability.

NET PROCEEDS.

The net amount realised from a sale, after deduction of all expenses of disposal.

NEWSPAPER PROPRIETORS, AUDITORS AND.

(See AUDITING, p. 115.)

NEXT-OF-KIN.

Those who are referred to under this phrase are literally the nearest of kin to any particular deceased person. If the words "in blood" are used as an addition, this means those who are next-of-kin in law. Generally speaking, the phrase denotes the person or persons who are entitled to succeed to the personal estate of a deceased, intestate under the Statutes of Distribution (*q.v.*).

NOMINAL ACCOUNTS.

These are such accounts as are of an abstract nature, and which, consequently, go under the names of the matters to which they relate, such as purchases, sales, discounts, commissions, wages, salaries, rent, rates, insurance, etc. Most of these accounts are those from which the Profit and Loss Account (itself a Nominal Account) is compiled. (See below).

NOMINAL CAPITAL.

The amount of capital with which a company is registered is known as the nominal or authorised capital. It is the amount stated in the Memorandum of Association, and upon this amount the capital stamp duty is payable. In addition, the nominal capital is stated in the Statement of Nominal Capital required by the Stamp Act, 1891, and subsequent Finance Acts, a document which requires stamping at the rate of 20s. for each £100 of capital. If it is desired to increase the nominal capital, this may be done as indicated in Section 41 of the 1908 Act. (See also LIMITED COMPANY ACCOUNTS, p. 636.)

NOMINAL LEDGER.

The Nominal Ledger is a separate Ledger containing all accounts necessary to guide the

NOMINAL ACCOUNT

Dr.				RENTS, RATES, ETC.				Cr.			
				£	s.	d.		£	s.	d.	
19..							19..				
Jan. 1	To Rates unexpired b/d			15	10	0	Jan. 1	By Rent accrued b/d			
Mar. 30	" Cash—Rent			25	0	0	June 30	" Water unexpired c/d			
Apl. 15	" " Water			2	5	0	" 30	" Transfer to Profit and			
June 30	" Rent accrued c/d			27	0	0		Loss A/c	66	15	0
				£69	15	0			£69	15	0
19..							19..				
July 1	To Water unexpired b/d			1	0	0	July 1	By Rent accrued b/d			
								27	0	0	

business in its profit-earning capacity, and from which the Trading and Profit and Loss or Revenue Account is compiled. Such nominal accounts comprise purchases, sales, carriage, wages, rent, rates, light, power, insurance, salaries, stable expenses, repairs to machinery, general expenses, commissions received and allowed, discounts, interest, bad debts, etc.

NONFEASANCE.

This is a legal term which signifies the omission to do something which ought to be done, and requires to be carefully distinguished from malfeasance and misfeasance (*q.v.*) which refer to acts of commission alone, either the doing of an unlawful act or the doing of a lawful act in an unlawful manner. The three terms are of importance in the law of torts as establishing the liability of the parties. Every private individual is liable for the acts caused by his malfeasance or misfeasance as well as for those caused by nonfeasance, but a corporate body can never be sued upon a tort which has arisen exclusively out of its nonfeasance.

NORMAL TRADE CAPITAL.

(See ACCOUNTS, CRITICISM OF, p. 19.)

NOTARY or NOTARY PUBLIC.

This is an official who, in a general way, certifies deeds and other documents. Originally his duty was to take notes or minutes, and to make drafts of writings. The name is derived from the Latin word *notarius*. His duties include—

(1) Attesting, copying, and translating documents, so as to render them valid when sent for use in a foreign country;

(2) Presenting dishonoured bills of exchange, and noting the fact of their non-acceptance or non-payment, and afterwards protesting them if required to do so.

NOTE BOOKS, AUDIT.

(See AUDITING, p. 72.)

NOTICE.

Certainty is one of the most important matters connected with the administration of law, and in order that this certainty may be attained, it is inequitable that any proceedings of a civil character—the same reasoning does not apply to criminal matters—should be carried through unless all the parties have had full opportunity of appearing in court, or have been made acquainted with the nature of the things in dispute. This is known as notice, and a notice may be connected with many different matters—notice of assignment of a debt, notice of an action, notice to admit documents, notice to produce documents, notice to quit, notice of trial, etc. Notice may be express or constructive; but in the vast majority of cases

constructive notice will not be sufficient to fix a person with knowledge. In every case, if possible, it should be express.

NOTICE TO TREAT.

This is a notice which is given under the Lands Clauses Act, 1845, when a corporation requires and is empowered to take for its operations certain lands, and is served upon all persons who are the holders of the land which the corporation wishes to purchase. Generally speaking, when a notice to treat has been given it cannot be withdrawn, and the corporation must go through with the matter. The effect of it is to constitute an inchoate contract between the corporation and the proprietors interested, the purchase money to be afterwards ascertained or agreed according to the mode provided by the Act.

NOTING A BILL OF EXCHANGE.

(See BILL OF EXCHANGE, PROTESTING.)

NOVATION.

According to the principles of the common law the only parties who could sue or be sued upon a contract were those who had originally entered into it. By degrees a creditor was allowed to assign his rights in special cases under certain statutory enactments, and eventually, under the Judicature Act, 1873, assignment became possible in every case, provided the proper steps were taken. But there is no such thing as the assignment of an obligation, except with the consent of the party to whom the performance is due; and if a creditor does accept a person other than the original party as his debtor, "novation" is said to have taken place. In fact, there is a new contract, and the old obligation is discharged. Whether there has or has not been a novation is a question of fact, and the difficulties that arise are mainly connected with changes created in partnerships, when one or more of the members of the firm retire, or where a company, such as an insurance company, has transferred its business to or become amalgamated with another company. (See also CONTRACT.)

NUDUM PACTUM.

A Latin phrase signifying "a bare agreement," that is, one for which there is no consideration (*q.v.*) and which is therefore unenforceable at law. This, of course, applies to agreements or contracts which are not under seal. If the contract is by deed, no consideration is required, unless it is a contract in restraint of trade, when consideration is essential, even though the agreement is under seal.

NUNCUPATIVE WILL.

(See EXECUTORSHIP ACCOUNTS, p. 447.)

OATH.

A SOLEMN assertion giving more binding effect to a statement or transaction in any proceeding than an ordinary statement. At one time the taking of an oath was only possible if made with Christian formality; but now in all legal matters a person is practically enabled to be sworn and to make a statement of a most solemn character in any manner which he considers to be binding upon himself. Even the act of "kissing the book" has been dispensed with by an Act which was passed in 1909. The penalties for perjury are nevertheless attached to false swearing, no matter in what manner the oath or its equivalent is taken.

OATHS, COMMISSIONER FOR.

(See COMMISSIONER FOR OATHS.)

OBITER DICTUM.

The meaning of this Latin phrase is "an expression thrown in by the way." The judgments derived in the High Court are always authoritative until varied or reversed by a superior tribunal; and in strictness the expressions contained in the judgments should be strictly relevant to the case in hand. Any casual remark thrown in by a judge, which though relating to the case is not strictly pertinent to the decision, is called an "obiter dictum." It cannot be cited as a strict judicial proposition in any sense, but there is nothing wrong in quoting it as an opinion.

OBJECTS OF LIMITED COMPANIES.

(See MEMORANDUM OF ASSOCIATION.)

OBLIGATION.

An obligation or a bond is a deed whereby a person obliges himself, his heirs, executors, and administrators to pay a certain sum of money to another at a fixed date. The person who so obliges himself or enters into such a bond is called the obligor; the person to whom he so obliges or binds himself is called the obligee.

The above is the correct legal meaning of the term obligation, but it is commonly used in a much more general sense as denoting any liability incurred by one person to another in virtue either of an agreement of the parties, or of their disagreement, or arising through some breach of a duty imposed by law.

OFFICE COPY.

This is a copy which has been made of an original document, examined with the original,

and certified by a responsible official as being correct. Thus, all wills are kept at Somerset House. The originals cannot be obtained. But a copy of a will is always forthcoming upon application and upon payment of the prescribed fees. An office copy is often known as a certified copy.

OFFICE EXPENSES.

Office expenses are a revenue charge, and, as they do not form a direct charge against manufacturing or trading, should be included, along with other similar establishment charges, as a charge against Profit and Loss Account.

Where apportionable charges such as office rent and rates, as distinct from factory rent and rates, are included under this heading, an auditor should inquire into the manner in which the apportionments are made. In most cases this heading applies only to postages, receipt stamps, and sundry petty cash expenditure.

OFFICE MACHINES AND APPLIANCES.

For the most part accountants and their clerks have been very slow to recognise the importance of modern appliances in offices, and frequently it is found that they are not cognizant of the machines that are available for accounting. Also some prejudice will be encountered in introducing machinery, but such an attitude on the part of the clerks especially should not be allowed to arrest the tide of progress. Accountants are often reluctant to call for detailed accounts and statistics concerning the working of their companies as they know that such work entails a vast amount of labour for their staff, and that unless it is extracted very carefully it is valueless. Machinery will enable much of this work to be accomplished in a mere fraction of the time required by mental or manual methods, and it is asserted that in a few years machines will do practically the whole of the routine work of an accountant's office and the clerks, generally speaking, will be employed on better work.

The principal machines suitable for accountants would appear to fall under the following heads—

- (a) Adding.
- (b) Calculating.
- (c) Book-keeping.
- (d) Cheque writers.
- (e) Tabulating.
- (f) Stamp affixing and coin counting and sorting.

It is proposed to describe very briefly the machines available under each of these heads so as to show some of the uses to which they can be applied, and it is hoped that sufficient description will be given to provoke an interest and consideration of the possibilities of their use.

ADDING MACHINES.—The adding machine is rapidly finding its way into offices and, next to the typewriter, is undoubtedly the machine most widely used. It is, however, a common impression that adding machines can only be used with advantage for totting of long columns of figures and many accountants who do not have a great amount of this class of work consider that the capital outlay would not be justified; but even a cursory examination of the capabilities of the adding machine will show how great are the uses to which the machines can be put, since, in addition to adding, they can be used for a great variety of purposes in which figures are required to be tabulated or checked.

Adding machines can be divided into two types: (a) a machine which adds on the depression of the keys and shows the total on the "register" in front (usually termed the non-listing machine); and (b) a listing machine which prints each item and the totals.

Non-listing v. Listing Machines. The machine that gives a printed record is much slower in operation than one that does not print, but in many instances a printed record of the details is required, and if original returns are tabulated direct into the summary sheets or schedules by the machine, the copying is saved and the risk of error in the copying is eliminated if the originals are called over with the tabulating sheet. For checking work and for casting the columns of figures a printed record is not necessary and the superior speed of the non-lister ($2\frac{1}{2}$ to 3 times faster) is a great advantage. In other cases, where a printed record is desired only for calling over or as evidence that the work has actually been checked, it is usually expedient to dispense with a printed record, though many people imagine that it is impossible to check without a printed record; this method is vastly inferior to the simple process of doing the work again on a non-listing machine. This recasting method is not only more sound, since it is generally acknowledged that proof reading of figures is difficult and subject to error, but is also much faster. For audit purposes there is no reason whatever for the use and retention of printed records of the casts, and the whole of the calculating work of an accounts branch should be carried out on non-listing machines, provided effective checks are introduced. Before installing either type of machine, careful consideration should be given to the capacities of each to do the work. Both have their advantages in their respective fields, but the non-listing type

has the additional advantage of being capable of use for calculating work.

Non-listing Machines. The most popular non-listing machine is undoubtedly the Comptometer. It is a very light portable machine, which can be manipulated on the desk at the side of the work to be cast. There are a number of models—the decimal, the sterling, the rupee, the annas and pies, and models for weights and measures or time. It consists of a keyboard of nine figures in each column marked 1 to 9. The operation of the machine is completed simply by depressing the keys—no auxiliary movements of any kind are necessary. The results of each calculation are shown on the register in front of the machine, and the totals are cancelled by touching the handle on the right. With a little practice it is possible to cast long columns at a very fast rate, and without the fatigue which usually follows this class of work when done mentally for long periods. The enormous amount of time that is saved is difficult to appreciate without actual demonstration.

There is a device special to the Comptometer known as the Controlled Key, which locks the whole machine when an imperfect depression of a key is made. The importance of the Controlled Key cannot be over-estimated, since it secures an accuracy which is impossible without it.

It is expedient to check all additions which are being done for the first time as, indeed, it is necessary to do when they are mentally cast, but checking on the Comptometer does not involve the labour which a mental check entails. It may, of course, often be considered unnecessary by accountants to check additions, when a cross-cast or other check is present, but there is always a risk of a counterbalancing error; commercially, this risk is generally taken with a skilled operator.

The Comptometer also subtracts, multiplies, and divides, and practically any arithmetical calculation may be performed by its aid.

The Burroughs non-listing machine is similar in many respects but differs in a few features.

Listing Machines. There are several listing machines available, but the Burroughs is the most popular machine. The listing machine records every item that is set, and when the total or sub-total key is struck it likewise prints it. These items are sometimes printed on a roll of paper at the back of the machine, and the strip of paper relating to any column or particular set of figures is torn off and used for record and checking purposes; but this is by no means the best use of the listing device, for it can be utilised for a large number of purposes by inserting forms, statements, looseleaf ledgers, account forms, schedules, etc., into the machine and tabulating in the necessary figures mechanically. It is also very useful for tabulating and totalising returns, invoices, wage cards, etc.

The machine is made in a very large number of models which are designed to suit all classes of work, and the operation of the machine is roughly the same whatever model is used and no matter into how many columns the data is tabulated. A large number of variations are possible with these models. In some models there is an unlimited split device which enables the keyboard to be divided into any number of adding sections, which can be arranged to print into the columns of a form or table. Another device enables the operator to print the number or date of a cheque, warrant, return, etc., by the side of the amount without including the former in the total. The "Duplex" or "upper and lower case" machine, enables debit and credit balances to be extracted in once going through the books, and the totals of each to be given. There is also an adding and subtracting model, which is largely used by banks and commercial houses for posting current account ledgers and statements. From the previous balance the machine deducts automatically the cheques drawn, adds the deposits, if any, and gives the balance in the balance column on the right-hand side. The speed at which these machines can be operated varies with the type of machine and the nature of the figures that are being handled. On an average 1,000 four-figure items can be listed an hour.

CALCULATING MACHINES AND APPLICATIONS.—The amount of time expended in the process of arriving at figures by accountants is generally very great and is frequently out of all proportion to the results obtained. Modern methods require the computation of more figures than were formerly necessary, and the desirability of substituting mechanical for mental labour in accounting work, therefore, assumes very great importance. There are three principal methods of calculating which claim to eliminate mental process in varying degrees—

- (a) By rating, ready reckoner, and specially constructed tables.
- (b) By slide rules.
- (c) By calculating machines.

Rating and Ready Reckoner Tables. The general utility of tables for calculations of all kinds is not always fully recognised. A careful perusal of all the tables now published demonstrates that some of the most complex calculations can be easily solved by their use, and for certain classes of work tables undoubtedly enable the results to be obtained quicker than any other method. All accountants having any kind of calculating work are strongly advised to consider the possible use of the tables—either using one of the many books of tables now published, or by having them especially constructed.

Slide Rules. Quite a considerable number of slide rules are used by accountants for certain

classes of work, e.g. where the figures handled are fairly small and where the results are not required to be carried out to minute accuracy; or where values are not involved, they are particularly suitable, and can be operated faster than many calculating machines. A slide rule in which a very large scale is got into a handy compass is the Fuller spiral or cylindrical slide rule, and many accountants employ this for costing, percentages, etc.

Calculating Machines. Calculating machines may be divided into three types—key operated, crank operated, and a combination of both.

The Comptometer and the Burroughs non-lister are the most popular of the key operated type and are suitable for all classes of calculations. This type of calculating machine possesses one salient advantage over other machines in that it can be used for all four rules of arithmetic. For practical purposes, crank operated calculators are useless for addition, and also listing machines are impracticable for multiplication and division.

The controlled key on the Comptometer eliminates entirely the error arising from imperfect depression of the keys. Speed of operation naturally follows practice, but the average clerk can, at the end of an hour's practice, multiply at least six times as quickly on the Comptometer as he could mentally. In addition and division the utility and speed of these machines is not fully appreciated until the operator has acquired a certain amount of skill. When installing a key operated calculator it is always advisable to employ a trained operator, in order to obtain the full value in speed of the machine.

Crank Operated Calculators. The crank operated machines may be divided into two types—the horizontal and the vertical. Most of the machines of this class weigh only a few pounds and can be operated on the desk and transferred from clerk to clerk. The *modus operandi* is so simple that any one of ordinary intelligence can use the machine after ten minutes' instruction, and proficiency and top speed of operation can often be attained in an hour. The operation of the machine merely consists of moving the levers or buttons on the dials, turning the handle, and sliding the carriage.

The horizontal type of machine is now becoming more popular than the vertical type—the Madas, Tim, and Layton's Arithmometer, being much quieter in operation and possessing advantages over the vertical type—Brunsviga, Muldivo, etc. In the Madas division can be accomplished merely by turning the handle until the carriage has travelled along until the number of places of decimals required in the answer has been reached. This device eliminates the necessity of mental work, obviates moving the carriage for each column, and makes division absolutely a mechanical process.

The Key and Crank Operated Machines. It has long been considered by calculating machine experts that the ideal machine would embody the principles of both key setting and crank operation. In the Millionaire and Monroe machines these features have been incorporated, though these two machines are not similar in construction or mode of operation. The Millionaire gives by one movement, for instance, that 6 multiplied by 6 equals 36, instead of by the method of adding six separate sixes together, involving six movements. The operation of this machine is entirely automatic, and consists of entering the multiplicand in one register by depressing keys, and as each figure of the multiplier is entered in a second register the product is simultaneously produced in a third register.

In the Monroe the numbers are set on a keyboard very similar to that of the Comptometer or Burroughs, and the calculations are performed by means of the crank at the back, having a two-way mechanism movement similar to the Brunsviga.

In selecting a calculating machine it is particularly desirable to consider the various types available, since the nature of the work is often the governing factor in the choice of a machine.

BOOK-KEEPING AND ACCOUNTING MACHINES.—It is common knowledge to accountants that many firms are suffering because of their inefficient book-keeping, and bankrupts often admit that their insolvency was caused by insufficient book-keeping or reliance on the annual balance sheet. Efficient management requires statistics in order that the maximum progress may be accomplished to achieve the maximum business. Careful inquiry into the reasons for the success of some of the largest concerns in this country shows clearly that it has been due in a great measure to the information which is periodically collected by the management as to the exact working of each department, and that the cost of supplying even the most detailed information to the executive is very small, because modern methods and appliances are employed in the offices. Book-keeping by typewriters and other machines may surprise many people, but in many of the largest firms the whole of the book-keeping is now done on machines. The machines will post ledgers, make statements, make up pay rolls, make out invoices and extract balances. Book-keeping is thereby reduced to the simple process of inserting the necessary sheets into the carriage of the machine, depressing the keys for the amounts, etc., and the details are printed and added on the sheet by the machine. Certain safeguards are provided to check the mechanical operation, and each amount added or subtracted is visibly recorded in a totaliser.

The *pay roll* is a very important item in the

counting-house of a large firm, and in some firms it represents the greater part of the outgoings. It must be accurate, for mistakes on a pay roll would not only be very costly and cause distrust of the counting-house by the employees, but are often untraceable. The Burroughs Adding Machine Co. recently conducted an investigation into the handling of pay rolls in 475 firms, and in spite of the different conditions that existed in the various offices, it was found that a considerable economy, amounting on an average to about 45 per cent., was effected over the mental method in firms where the machine was used. If the application of machinery to this class of work simplifies it and reduces the cost it should receive consideration.

It is not asserted that machines will eliminate entirely ordinary hand book-keeping in all spheres of business, though some machine enthusiasts assert that all book-keeping is machine work. It is well known that quite the greater part of the accounting consists in the handling of large cumbersome books, the searching for the page, the insertion of the items, blotting, etc., which occupy a large amount of time, while errors in copying are easily made and occasion an inordinate waste of time to rectify.

The Elliott Fisher. The Elliott Fisher is a very widely used book-keeping machine, and offers the means of performing every operation in any class of book by machine. The Burroughs method of book-keeping does not enable the matter to be itemised, nor does it allow any text, except a few set terms, to be written up. The Elliott Fisher consists of a flat stationary bed over which operates a typewriter with adding and other special attachments. When the actual books, or the loose-leaf sheets of the books, or the invoices, etc., are placed on the flat bed of the machine, the typewriting mechanism may be moved about and the text and figures inserted at any desired point on the sheet. The flat bed of the Elliott Fisher makes it a splendid manifold, and also enables the machine to write into bound books, cards, etc., of almost any dimensions. The adding registers which are fitted, automatically collect the figures to be totalled; each register records only the figures typed in its particular column, and, although it is a fixed part of the machine, it can be made operative or inoperative by means of a lever.

The most recent improvement in accounting machinery is the Crossadder. This adjunct to the machine adds or subtracts across the columns as well as vertically, and at the end of each line the total is printed, and if the entries have been correctly typed, the Crossadder automatically clears.

It is obviously impossible to lay down any general rule as to what classes of book-keeping

are best done by machines, for the nature of the business and the size of the concern must be taken into consideration, so that every counting-house must be considered on its merits.

Invoicing and "Billing" Machines. The typewriter with special attachments, or the Elliott Fisher, is now almost universally used for "billing," as it enables all the necessary records to be written at the same time, and each record is, of course, the same, thus securing uniformity and accuracy of work. The "billing" may consist of producing a copy of an order for the factory or warehouse, the sales manager, the cashier, the loose-leaf sheet of the Day Book, and for any other department of the business; also the customer's advice and the address wrapper or label may be included. Simultaneously with the making out of the orders the machine will collect the figure items and add them so that the totals can be inserted where necessary.

The Elliott Fisher Invoice Adding machine is particularly adapted for "billing." The flat stationary bed of this machine possesses exceptional manifolding powers and enables a large number of duplicates to be made at one writing. By using a number of forms arranged in the same registration, a large amount of detail work can be concentrated into one operation.

The Wahl Adding and Subtracting Attachment. The typewriter and adding machine have long occupied two important positions in the office, but, although they can be regarded as necessary twins, they have not overlapped in their functions, although the work which they each perform overlaps. They have really been required to work side by side, since the ordinary typewriter does not add and the adding machine does not write. The Wahl attachment, however, which can be built in certain makes of typewriters, enables figures that are typed into various columns, etc., to be added or subtracted. The process of typewriting does not require to be modified in any way, and a number of safeguards are included which make the machines almost "fool-proof." The totaliser can be set to any point along the carriage, and if it is desired to add any number of columns simultaneously, an extra totaliser for each column will be required.

CHEQUE WRITERS.—The number of cheque frauds that take place is far greater than is generally supposed, for only in a limited number of cases is it possible to take proceedings and bring a report of the case to the notice of the public. Further, it is unnecessary to point out to accountants that cheque frauds are generally carried out by highly skilled criminals, and in spite of the special surfaced paper on which cheques are generally printed, and the fact that the cheque form is often printed in an ink that is more easily removed than ordinary writing ink, it is possible

for an expert to remove "crossings" and line over any part of the cheque that may have been destroyed, and to alter the amount.

There are several cheque writing machines available—the Protectograph, the Elliott Fisher, and the Safeguard. The Protectograph prints in two colours the amount for which a cheque is drawn. It writes a complete word at each turn of the handle and the operation is undoubtedly faster than writing. The salient feature of the machine is that it crushes or shreds the words, and thereby forces the indelible ink into the fibres of the paper, thus rendering subsequent falsification by mechanical or chemical means impossible. The amounts are written in red and the denominations (£ s. d.) in black. The operation of the machine is very simple, and with a little practice cheques can be made out more quickly than by hand writing. The machine method of writing cheques gives uniformity and neatness to all cheques, and ensures that they are protected before final signature. The machine will also crush a "Not negotiable" or "Account payee only" crossing, and it will take any size cheque.

In the Elliott Fisher the protection is secured by the use of a "pin point type," which makes a printed and perforated impression on the cheque, and writes the whole of the cheque except the signature. By arranging the cheques in books with, say, four to a page and inserting the counter-foils behind each page of cheques, a facsimile of every cheque made out is obtained and the totals are collected and can be posted to the Cash Book.

In the Safeguard Cheque Writer the payee's name, as well as the amount, is protected by shredding or perforating the name after it has been written in ink. The Safeguard writes and shreds the work diagonally—each word commencing under the previous word which allows very large amounts to be written in a bold type on one line.

TABULATING MACHINES.—The Hollerith and Powers Tabulating Machines are not very widely known or used for accounting work. At the outset it is not asserted that this class of machine is suitable for all accounting work, for much of such work can be performed more economically on the adding machine; but where the data to be tabulated is of a complex nature, consisting of a number of factors that are required to be tabulated in a number of categories, the Hollerith and Powers systems are of special utility. The machines were originally designed to tabulate census figures, but their adaptability for business purposes is rapidly becoming known, and they are being profitably employed for costing work, sales analyses, and many forms of accounting work.

It is not possible to convey a complete idea of the capabilities of these systems, but their fundamental principle is to record information that it is desired to tabulate by punching holes on cards, which are thus rendered capable of mechanical manipulation. The punching of the cards is equivalent to entering the facts into books or on to cards by hand. The cards are printed with a series of figures in forty-five columns and a group of these columns is taken to record information concerning any particular item. Thus, to record 245 tons of any commodity a hole would be punched over a figure 2 in the hundreds column, another hole over figure 4 in the tens column, and another hole over figure 7 in the units column. The holes are perforated in the cards by means of a punching machine and the rate at which the cards can be punched varies with the number of columns and the skill of the operator, and may range from 300 to 800 per hour.

The next process is to arrange the cards in the necessary order, and this is accomplished by sorting them according to the holes punched in the various columns. This is done in the sorting machine—the position of the holes in the cards causing them to fall into various receptacles.

The tabulating or adding machines differ very considerably in the Hollerith and Powers systems, although their functions are analogous, that is, to obtain the totals of the various factors. The totals can be obtained from any division of the cards. The Hollerith machines total 9,000 cards per hour, and if the five counters are being used this represents 45,000 items, while the Powers' machine prints the items and totals 3,500 cards per hour.

It is impossible to say that either system is better than the other. While the main principles of both systems are identical, each has its special features and advantages, which may or may not be of special utility to the work required to be done. Accountants should, therefore, consider both systems, for it is not even possible to postulate that one system is particularly suitable for, say, costing. The choice will generally depend on the form in which the data is finally required; in other words, the tabulator will usually govern the system adopted. For general consideration the punching and sorting may be regarded as equal on both machines, although if the work of punching is likely to be decentralised the Hollerith puncher will be more economical. The main difference in the sorters of the two systems is that in the Hollerith the whole mechanism is actuated by electrical contact as against mechanical contact in the Powers. The tabulators should receive the most careful consideration, for they will probably determine which system is to be adopted.

The machines can be applied to the general accounting and book-keeping system of the business, and are of special use in the important phase of accounting cost keeping. The systems are undoubtedly capable of enormous development as they permit of great adaptability for accounting and statistical data. It should be noted that both companies undertake all classes of statistical and accounting work for firms.

STAMP AFFIXING MACHINES.—The affixing of postage stamps by the usual office methods is rather slow and messy, and the necessary records in the Postage Book occupy some time. Stamp affixing machines are now available that will efficiently affix stamps of any value. A recorder counts every stamp and the machine can be locked so that the stamps can neither be affixed nor removed. Apart from the fact that these machines constitute a real labour-saving device, they enable the work to be performed more hygienically and prevent the possibility of pilfering. The pilfering of postage stamps is a matter of greater importance than is generally conceded, and the introduction into the organisation of a system that eliminates the possibility of the temptation to use the stamps is also a safeguard. The use of the postage record book is then unnecessary, or, if kept at all, only very short consolidated entries are required. Several accountants, however, still insist on the retention of the stamp record for purposes of reference and as a double check. The stamps for these machines are obtained from the Post Office in rolls of 500. Another use to which these machines have been very extensively applied is for affixing Insurance and Unemployment stamps. The machine affixes, cancels, and counts by merely pressing down the handle, and as many as 100 cards can be stamped in a minute. The most popular machines on the market are the Multipost, the National, and the Standard.

COIN COUNTING AND SORTING MACHINES AND APPLIANCES.—The automatic silver sorter consists of a series of sieves, the mesh of each tray being such as to retain only one particular denomination. When a quantity of mixed silver is emptied into the top tray, a little shaking causes the coins to fall to the tray the mesh of which is small enough to hold them. A more rapid method of sorting is accomplished with the Rapid Coin Sorter. The mixed coinage is poured into the tray, and by turning the handle or using an electric device, the coins fall into separate bags according to their denominations. The International Coin Counter consists of a horizontal rotating disc in which are holes of the size which will receive only one coin of the denomination which is to be counted. Each coin as it passes from the opening of the disc engages a small spindle which moves the index of the counter. When the required

number of coins have passed, the machine automatically stops and the coins are packeted. The Burdick Coin Counter is made in hand and power operated models, and counts and totalises silver coins of all denominations. These machines are used in several banks and large firms, as counting by hand is not only slow and involves much drudgery, but requires to be checked in order to ensure accuracy.

All the above machines, together with addressing, folding, envelope filling and sealing, duplicating, photo-copying, time recording, job costing, etc., machines, are dealt with very fully and particulars given of the names, etc., of all types available, in *Office Machines, Appliances, and Methods*, published by Sir Isaac Pitman & Sons, Ltd., Parker Street, Kingsway, London.

OFFICE ORGANISATION AND SCHEMES OF INTERNAL CHECK.

If we classify in general terms the numerous descriptions of trade, manufacture, and professions, we shall probably find that as between the members, as it were, of each family or category, there is more or less a mode or system in principal essentials common to each class, and that schemes of organisation in a class primarily differ from each other more in matters of detail than in questions of principle. The precise organisation of any business, however, depends *inter alia* upon its nature, size, ramifications, routine and conditions, and its existing form, in so far as it may have deflected from that which witnessed its inception or its early history, is traceable to the permutations, vicissitudes, and changing scenes through which it has passed, and may continue to pass, in the prosecution of its objects. Some lines or classes of business are by their constitution and circumscription not subject to much change as regards principle or detail; to others, time may apply such terms as evolution and metamorphosis.

A factory or other business of similar kind and significance may be broadly divided into general administration; sub-divided into finance administration, works administration, and sales administration; which may be composed of the following elements: board of directors, general manager, secretary, accountant, sales manager, works manager, chief designer, draughtsmen, travellers, buyers, works accountant or cost accountant, financial manager, cashier, foremen, timekeepers, storekeepers, tool designers, wages and other clerks, plant and machinery engineer, inspector, rate-fixing committee or department, warehousemen, and others, according to the conditions of each particular case. On the other hand, if we take the office of a secretary or administrator to many companies of different kinds operating abroad, we have, in London, the boards of directors,

secretary of the companies, accountant, correspondence department, transfer department, general clerks; and abroad, in the service of each company (possibly), local directorate, general manager or engineer, as the case may be, and the usual staff.

What is known as a system, or scheme of internal check, is essential to the due performance or carrying out of the details of all companies with large and growing commercial operations. It constitutes an indispensable part in the construction of organisation and in operations of number and magnitude. Its effectiveness depends upon the soundness of the system itself and the efficiency of its practical application. Various kinds of internal check may be inaugurated, according to the precise object to be achieved, all forming component and harmonious parts of the complete system of check instituted.

A system of internal check is sometimes defined as a limited kind of audit. It is not a happy definition; but it probably sufficiently indicates the meaning. Its chief functions are to prevent collusion and fraud, to secure correctness in book-keeping, accounting, and other records, and where an effective system is in force, and is efficiently applied, the work of the auditor is correspondingly facilitated and benefited.

In large concerns, where there are perhaps numerous Sale Ledgers and sectional balancing is in vogue, it may be the practice to extract the Ledger balances monthly, and for the postings to be checked by clerks other than the book-keepers themselves, the debits and credits and the balances being indicated in a Balance Book or on suitably designed sheets.

The controlling accounts of these Ledgers will be kept in the private office, and the controller, or person in whose custody and use they are, will be able to verify the aggregate balances of each Ledger in the manner following—

The ledger clerk will post his debits and his credits of any return of goods from subsidiary books or slips of prime entry, and he will post the cash from the General Cash Book (which will be kept by another clerk), and any bills from the Bills Receivable Book, which will be kept in the private office. The controller will obtain his debits and credits of goods for each Ledger from one or more prime sources (which may be easily created) quite independently of each ledger clerk. The cash and discounts for each Ledger will appear in totals in the Private Cash Book, the General Cash Book being designed to this end and analysis, and at the end of each month he is in the position of knowing the balance of each Ledger. Moreover, monthly statements of account may be rendered to customers by the private office with forms of acknowledgment requesting notification of the correctness or otherwise of

such statements of account, they being entirely dealt with by the private office: *e.g.*—

CONTROLLING ACCOUNT.—A LEDGER.

To Cash	£ 5,000	By Sales	£ 10,000
" Discounts	100		
" Bills Receivable	200		
" Returns	50		
" Balance	4,650		
	<u>10,000</u>		<u>10,000</u>
		By Balance	4,650

The suggestions indicated are, of course, part of a system of sectional balancing and efficient internal check.

Similar effective checks may be instituted as between transfers of manufactured stock *ex* factory to warehouse, deliveries *ex* warehouse, and in many other directions.

With regard to the receipt and payment of cash, various devices or modes obtain. Let us consider the following phase. A B & Co. are music publishers (retail and wholesale) with a large central warehouse and shop, and an organisation of travellers. The travellers receive a regular salary, commission on orders, and expenses on scale.

As regards the shop, the assistants who supply the retail customers prepare carbon invoices, which are handed to the customers, who pay at the cash desk for what they have purchased. The supply of goods and the payment thereof are thus kept quite distinct.

As regards the travellers, the *modus operandi*

in vogue in the particular instance in mind, cannot claim to be ideal, but, combined with the means of inspection, control, and guarantee, in operation it seems to satisfy the requirements of the situation. As received, the travellers in various parts of the country transmit their orders to London for execution, an invoice being sent direct from the office to the customer. At the end of each month each traveller sends his account to the head office somewhat as shown below.

The weakness of the system is that the travellers receive cash from customers ; but in this particular instance it is unavoidable. Out of their cash collections, they pay themselves their salaries, commission and expenses, remitting the balance to London at the end of the month, with an account drawn somewhat as follows—

	£	£
Total amount of receipts as above		....
Deduct salary for the month .	....
Expenses, as per Expenses		
Statement and Vouchers		
attached . . . .	....
Commission on orders for the		
month . . . .	....
	<hr/>
Balance remitted to Head Office		....

When the takings of the travellers are insufficient to pay the salary, expenses and commission, a sum is thus due from the office to the travellers, which means a remittance from

STATEMENT OF ORDERS RECEIVED AND TRANSMITTED TO LONDON DURING
THE MONTH OF JANUARY, 19..

[illegible]

.....Date.

.....Traveller.

CASH RECEIPTS DURING THE MONTH OF JANUARY, 19..

[illegible]

London. These cash accounts are rigidly checked, the expenses allowed being on certain definite lines.

At the end of each quarter a statement of account is rendered from the London office to each customer, to which is attached a special form requesting an acknowledgment of the correctness or otherwise of the statements.

Controlling accounts may be created in and applied to almost all kinds of commercial transactions and circumstances. As a further example, they will be familiar to those who have to deal with the accounts of undertakings owning a number, or possibly a large number, of steamers engaged between regular ports in passenger and cargo transport.

We need refer only to the latter. Controlling accounts are commonly raised with the freight department, which deals with the ocean freight on both inward and outward voyages, a controlling account being opened for each voyage, which is debited with the amount of freight as shown by the cargo or freight manifests (which are prepared from the Bills of Lading), and correspondingly credited with the cash payments on collections in respect thereof. The balance of each outward and inward voyage controlling account will, or should, agree with the aggregate balances of the individual detailed accounts, and shows, of course, the amount of freight outstanding from time to time. Similarly in regard to ocean passage revenue. Sometimes the freight on goods is payable at home and sometimes abroad, for which provision is made in the accounting as it is also made for (1) estimated freights (*i.e.* amount of freight estimated *pro tem.* until the out-turn is known); (2) "through-rate freight," in which case a portion of the freight must be credited to the railway company; and (3) "intermediate freights," that is, freights between ports of call or intermediate ports on the outward and return voyage.

Those who have had experience in railway accounting will be familiar with the terms "paid on," "to pay," "paid," and "through." The "paid ons" represent payments made or to be made in respect of the carriage or freight of goods to be charged to the consignee.

Costing may be defined as any systematic record of expenditure incurred in production, output, construction, or services rendered. The costing of the merchant who merely sells what he buys, with no intervention on his part of wages, materials, and expenses of maintaining a factory or workshop, need not be discussed, since it requires but little system or record to arrive in his case at the essential information. The installation of an efficient system of costing means a previous close study of the conditions, routine, and organisation of the business to which it is to be applied, including its departmental and inter-departmental methods and relations. To be of practical utility,

there must not only be regularity in critical examination by those responsible, but the information must be presented in suitable form and detail, all of which pre-supposes that the system to be installed should possess, as far as it is possible to obtain them, clarity and simplicity. It is, however, to manufacture, or production which involves outlay in wages, material and expenses, that costing more immediately and in particular applies itself.

Broadly, the businesses or undertakings in which costing plays a prominent part may be classified as follows—

1. Businesses or industries composed of a number of separate departments, each department dealing with a distinct description of output of goods, the objective being the cost of each department and each description of goods.

2. Undertakings in which the cost of working is expressed in terms of a standard or unit. For instance, an electric tramway company, in which the costs of operating or working are expressed per car mile run, or an electric lighting company, in which they are expressed per B.O.T. unit sold, generation costs per unit generated, and so on.

3. Contracting and constructing businesses, in which the object to be attained is the cost of each contract; a shipping company, the cost of each outward and inward voyage.

4. Businesses, the output of which consists of a number of separate articles or descriptions of manufacture, each article or description necessitating certain processes in which it is desired to exhibit the cost of each department, the cost of each process, and the complete cost of the finished article or product.

The elements of costing are wages, materials, and expenses, or oncost, the latter being also known by the terms burden or overhead expense. The expenses may be direct or indirect. Prime, first, or flat cost, is in some cases taken as representing wages and materials only, and in others it is taken as shown in the following form—

Wages	.	.	.	.	.	.	£
Materials	.	.	.	.	.	.	....
Direct expenses of production	.	.	.	.	.	.	....
Indirect expenses of production, such as							
Wages of Superintendents, Rents,							
Taxes, Insurance, Lighting, Depreciation and maintenance of Plant and							
Buildings	.	.	.	.	.	.	....
<hr/>							
= prime cost.							
Expenses of administration and distribution	.	.	.	.	.	.	....
Profit	.	.	.	.	.	.	....
<hr/>							
= selling price.							

Oncost consists of expense partly variable, it

may be according to quantity of saleable production; and partly permanent, irrespective of production. This permanent oncost often occupies a place of considerable importance in the complete or total cost, and as a general observation the tendency is for it to increase.

The subject of recording labour or wages is associated with time-keeping and allocation, and where there is a large number of men employed, there should be an efficient system of recording the time, service of labour, and the precise work upon which it has been expended, for the purpose of the periodical pay bill and for the ascertainment of the cost of the work done.

There are in operation various modes or systems of remunerating labour.

The day work, or time work, method may be described as a method of remunerating labour by eliminating the quantity of work done. We may have such a system, either in whole or in part, (1) by which each workman of a class receives the same rate of wages; (2) by which the work to be carried out is more or less continuous, being carefully schemed and a record kept of the work done, the wages being determined on these lines.

The chief weaknesses of the day work system are (1) the efficient receive no more than the inefficient; (2) no incentive to improve methods of working, and, consequently, increase production.

Broadly, the piece-work system denotes all those various methods or schemes for remunerating labour on the basis of the amount of work performed instead of on the time expended.

The differential piece-work system consists of a high rate per operation or piece, if a certain output in a given time be effected, and a lower rate per operation or piece, if the output be less than the standard set.

Fixed piece-work rates may be applied to those cases in which the rates are not subject to "cutting" or reduction.

Analytical piece-work rates signify rates applicable to convenient sub-divisions of work.

The contract or sub-contracting system describes those few cases in which the foreman or other responsible person contracts to carry out the work (the company finding the material) for a given sum, the responsible person making his own arrangement with the men. Usually, however, there are certain stipulations in the contract dealing with the rates of wages and other matters.

The piece-work method is, of course, an improvement upon that of the day or time work, and satisfies the requirements of certain classes of labour. It has proved, however, a fertile source of rate cutting or rate reduction and consequent industrial strife.

The selling price of production has its limitations as regards reduction. On the other hand, the wages of a piece-work man, of course, increase as

he becomes proficient, and circumstances may arise in which the employer, when he is unable to effect certain economies in material and oncost, reduces the rates he is paying to meet trade competition. The result is obvious; the workman curtails his efficiency accordingly.

The premium or bonus system (of which there are various forms in vogue, differing in principle from each other mainly in the details giving effect to it and in the apportionment of the bonus representing the value of the intensity of premium labour) may be noted.

The principle of this description of remuneration is intended to

(1) increase production;

(2) increase wages, and thus stimulate the employees to show increased interest in their work;

(3) produce a wider margin between manufacturing or productive wages and production; and

(4) produce a smaller ratio of oncost to production.

A rate-fixing committee or department is usually created which *inter alia* determines the standard times for various operations.

Some of the applications are—

Time rate: 9d. per hour
Standard time: 100 hours
Time occupied: 90 hours

$\frac{1}{3}$ of premium credited to workman

90 hours @ 9d. = 810

$\frac{1}{3}$ of 10 = $3\frac{1}{3}$ hours @ 9d. = 30

Wages . . . 840 pence

or 9.33 pence per hour.

If we take half of saving, we have—

90 hours @ 9d. = 810

$\frac{1}{2}$ of 10, the intensity of labour = 45

= 5 @ 9d. = 45

855 pence

or 9 $\frac{1}{2}$ d. per hour.

Or we may have a system in which the monetary value of the premium bears the same relation to the ordinary wages due for the time taken to complete an operation, as the time saved bears to the time allowed.

Premising as above, we have—

Time saved: 10 hours } = $\frac{1}{10}$
Time allowed: 100 hours }

Pence.

9 hours @ 9d. = 81

90 hours @ 9d. = 810 = $\frac{1}{10}$

891

$\frac{891}{90} =$ rate per hour

In some cases the payment of the premium may not be made until say 5 per cent. premium

has been earned, and probably in multiples of 5 per cent. thereafter, or we may have the cardinal principle that the workman be paid a certain rate below the standard for his intensity of production.

Following the previous examples, we may proceed—

90 hours @ 9d.	= 810
10 hours saved, payable at, say, 7d.	= 70
	<hr/>
	880 pence

and $\frac{880}{90} = \text{rate per hour}$

Rules are made as to defective output due to inferior material and as to workmanship. It is usually provided that if a man's work does not pass inspection, he receives no premium for the work or operation unless he is able to make it good in the standard time, in which case, if he does so, he, of course, becomes entitled to the premium which he has earned.

To each workman is issued a job or premium card somewhat as in the form below, which is filled up in part by the drawing office, rate-fixing department, foreman or timekeeper, shopinspector, counting-house or costing department.

The card may be accompanied by a stores or materials card, in which are set forth the materials required and which enables the workman to obtain his requirements accordingly.

Some phases of a system that pertains to the internal working of a large store may be noted,

as, for instance, the inward or purchase invoices, which are "marked off" on the copies, counterfoils, or other records of the orders or contracts placed, and upon which the executive committee or the department exercises continuous check and vigilance. The buyer, or responsible person of the department concerned, certifies the invoice for such lines or items as are his portion, with the distinctive indication of the department. The details of the invoices, such as prices, calculations, additions, extensions and discounts, are checked, the invoices bearing the initials of each person concerned in the performance of the check. The invoices are entered in the Purchase Journal or Bought Invoice Book kept in the office, and are analysed in the dissection office or department. The totals, either weekly or monthly, of the dissection office are agreed with the totals of the Inwards Invoice Book. In the dissecting department the invoices are dissected daily in a Purchase Dissection Book, the totals of which are transferred weekly, monthly, or at the end of any other period, as may be the practice observed, to the summary of Purchases Book, which, as its name implies, is a summary of the Purchases Dissection Book (spaces being allotted for each department), and, as we shall see presently, it is also the receptacle for the analytical totals of the sales of each department, with additional columns for the record of other information. The dissecting or Analysis Book may assume the form shown at the bottom of page 729.

PREMIUM CARD

No. of Workman	Name	Rate	Standard Time
Operation			
Job No. Reference to Drawing, etc.			
Date and Hour of commencing work	Initials		
Date and Hour of completion	Initials		
Time taken	Initials		
Time saved	Initials		
Time taken	hours @	£	: :
Premium		£	: :
Overtime		£	: :
Allowances		£	: :
TOTAL		£	: :
Calculated by	Checked by	Initials	
Work passed	No. of operations		
	or pieces passed		

SUMMARY BOOK.—DEPARTMENT A

Month. (1)	Stock. (2)	Purchases. (3)	Transfers. (4)	Total of Purchases and Transfers. (5)	Estimated Profit on Sales at 40 per cent. (6)	Total of columns (5), (6) and (7). (7)	Month. (8)	SALES.		Total. (10)	Transfers. (11)	Total. (12)	Estimated Stock. (13)
								Ca h. (9)	Credit. (9)				
19.. Jan.	£ 5,000	£ 2,000	£ —	£ 2,000	£ 800	£ 5,000 2,800	19.. Jan.	£ 2,000	£ —	£ 2,000	£ 750	£ 2,750	£ 5,050
Feb.	—	3,000	1,000	4,000	600	4,600	Feb.	500	1,000	1,500	—	1,500	8,150
Mar.	—	5,000	—	5,000	2,000	7,000	Mar.	3,000	2,000	5,000	—	5,000	10,150

Transfers of goods from one department to another may be dissected from the transfer forms into a Dissection Book, as shown below, or they may be included in the first-named Dissection Book.

The returns of purchases, or returns outward, are entered in the usual type of Returns Outward Book, which is periodically dissected into the Dissection Book and shown in red ink at the foot. The Summary Dissection Book, which, as we have seen, contains the summarised records of each

department separately, may be designed in the form given above—

It will be noticed that the totals of the purchases, less returns, are transferred periodically from the Dissecting Book to the debit or left-hand side of the departmental accounts in the Summary Book, the columns 1 to 5 inclusive being self-explanatory.

The sales, both cash and credit, are dissected in a similar manner from the carbon sheets or invoices which bear the name or distinctive mark of the department concerned. The daily total of these

DEPARTMENTAL TRANSFERS

TRANSFER NOTE.				FROM.						TO.					
Date.	Brief Particulars.	Details.	Total.	Dept.	Dept.	Dept.	Dept.	Dept.	Dept.	Dept.	Dept.	Dept.	Dept.	Dept.	Dept.

DISSECTION, OR ANALYSIS BOOK

No.	Date of Entry.	Date of Invoice.	Name.	Brief Particulars.	Details of Amount.	Total.	DISSECTION.						TOTAL.
							Dept.	Dept.	Dept.	Dept.	Dept.	Dept.	

carbons must agree with the cashier's daily receipts, subject to receipts in payment of credit accounts, there being a connecting link in the organisation between the cashier and the office or counting-house.

The returns of sales, or returns inward, are abstracted or dissected from the Returns Inward Book in the same manner as the returns outward, and deducted from the sales.

The carbon slips, which are duplicates of the accounts given to the customers, after being dealt with by the office, find their way to the dissecting department, where they are dissected. These dissections are performed and entered daily in the Sales Dissection Book, the totals being transferred to the credit of the various departments to which they relate in the Summary Book, which contains the totals of purchases and sales of all the departments. The Sales Dissection Book may be in the form shown below.

Reverting to the Summary Book, its records show the following results—

JANUARY					
Stock	£		Sales	£	
Purchases	5,000		Transfers	2,000	
Estimated Profit	2,000		Estimated Stock	750	
	800			5,050	
	<u>7,800</u>			<u>7,800</u>	
FEBRUARY					
Estimated Stock	£		Sales	£	
Purchases	5,050		Estimated Stock	1,500	
Transfers	3,000			8,150	
Estimated Profit	1,000				
	600				
	<u>9,650</u>			<u>9,650</u>	

MARCH			
Estimated Stock	£	Sales	£
Purchases	8,150	Estimated Stock	5,000
Estimated Profit	5,000		10,150
	2,000		
	<u>15,150</u>		<u>15,150</u>

Estimated profit—January	£
February	800
March	600
	2,000
	<u>£3,400</u>

which may be shown in one account as under—

Stock	£	Sales	£
Purchases	5,000	Transfers	8,500
Transfers	10,000	Estimated Stock	750
Estimated Profit	1,000		10,150
	3,400		
	<u>19,400</u>		<u>19,400</u>

These outlines may be considerably amplified according to the requirements of the management. For instance, it may be desired to show the wages and expenses, and charges both direct and indirect, fairly chargeable to each department. This necessitates a combination of ascertained fact and assumption or estimate—as, for example, the equitable apportionment of certain charges, such as light, rates, printing and stationery, rent, salaries and wages, and other miscellaneous forms of revenue expenditure, and the consideration and preparation of a scheme giving effect as far as possible to the individual departmental fitness of things. Some of these expenses may be allocated on the basis of the turnover, wages, salaries, rent; but the subject is one that requires much careful detailed consideration.

SALES DISSECTION BOOK.—WEEK ENDED.....19....

Department.	MONDAY.			TUESDAY.			WEDNESDAY.			THURSDAY.			FRIDAY.			SATURDAY.			TOTAL.		
	Cash.	Credit.	C/Acs. paid.	Cash.	Credit.	C/Acs. paid.	Cash.	Credit.	C/Acs. paid.	Cash.	Credit.	C/Acs. paid.	Cash.	Credit.	C/Acs. paid.	Cash.	Credit.	C/Acs. paid.	Cash.	Credit.	C/Acs. paid.
1																					
2																					
3																					
4																					
Etc.																					
Deduct Returns																					
TOTAL																					

NOTE.—A column should be provided under each day for the total of Cash and Credit Sales. As already indicated, the totals are transferred periodically to the Summary Book. It should be noted, however, that the payments or receipts in respect of Credit Accounts (C/Acs. paid) are not entered in the Summary Book, these being dealt with by the office when they are credited in the Sold Ledger.

Sometimes it may be that the trader prefers to record the gross departmental profit in cash.

It will be gathered from the above observations that controlling devices or means of internal check may be devised for all kinds of businesses, and that the greater the independence of the check or device, the greater the satisfaction derived therefrom.

OFFICIAL ASSIGNEE.

One of the several members appointed by the committee of the Stock Exchange every year to examine the books, to investigate the circumstances, and to manage generally the affairs of any member of the Stock Exchange who has been declared a defaulter (*q.v.*). All the business is carried out in accordance with the rules of the Stock Exchange.

OFFICIAL RECEIVER.

A public official appointed for one of the districts into which the country is divided for the purposes of the administration of the Bankruptcy Acts, to inquire, in the first instance, into the affairs of an insolvent person or of a joint stock company in the early stages of the insolvency or the winding up. Immediately a receiving order has been made against a debtor, the Official Receiver becomes the holder of the debtor's estate and he acts as protector of the same until a trustee in bankruptcy is appointed, if the debtor is, in fact, adjudicated bankrupt. In the same way, he acts as protector of the estate of a joint stock company which is being wound up, until a liquidator is appointed. And if at any time there is a vacancy in the trusteeship or the liquidatorship, as the case may be, the Official Receiver acts during the period of the vacancy. In the case of small bankruptcies, the Official Receiver frequently acts throughout, and he then occupies the position of trustee without the intervention of any other person. In all his actions the Official Receiver is under the control of the Board of Trade.

The duties of the Official Receiver may be summarised as follows—

1. **BANKRUPTCY.**—He is concerned with the conduct and the property of the debtor. As to conduct he must—

(a) Furnish the debtor with all necessary instructions and forms for the preparation of his accounts.

(b) Investigate whether the circumstances are such as to make the debtor guilty of any of the offences set out in the Debtors Act, 1869, as amended by the Bankruptcy Act, 1914.

(c) Report on the conduct of the debtor during the bankruptcy inquiries, and supply such information as will influence the court when the debtor applies for his discharge.

(d) Take such part as is necessary in the

public examination of the debtor, either personally or by means of a solicitor or counsel.

(e) Direct the prosecution of a fraudulent debtor, if such a course is considered necessary, in such manner as the Board of Trade directs.

As to the debtor's property, his duties, in addition to those already mentioned, are—

(a) To authorise any special manager to raise money and make advances for the purposes of the estate if it appears beneficial to do so.

(b) To summon and to preside over the first meeting of creditors, and to make known any scheme of arrangement proposed by the debtor.

(c) To advertise all the proceedings which are required to be so done by statute.

(d) To render full accounts of all matters connected with the estate to the Board of Trade.

Whenever he acts as trustee, he has all the powers of a trustee in bankruptcy (*q.v.*). In his official capacity he has full power to administer oaths for the purpose of affidavits, for verifying proofs and petitions, and for all other proceedings under the Bankruptcy Acts.

2. **COMPANY WINDING UP.**—Besides acting as liquidator until a regular appointment is made, as already noticed, the duty of the Official Receiver is to require a statement of the affairs of the company from the officials, and in order to secure this, he must provide the proper forms required by statute. He then prepares a report, setting out in detail all the matters connected with the company—its promotion, formation, career, and the causes of its failure. In certain cases he must report upon the conduct of the officers of the company, especially if there are any suspicious circumstances which require investigation. As in bankruptcy, the Official Receiver summons and presides over the first meeting of the creditors (he also presides over the first meeting of the contributories), and takes part in the public examination into the affairs of the company, either personally or through a legal representative. In connection with companies, as with bankrupts, he is entirely subordinate to the Board of Trade. (See also **BANKRUPTCY ACCOUNTS**, p. 179.)

OFFICIAL RECEIVER'S ACCOUNTS.

(See **BANKRUPTCY ACCOUNTS**, p. 179.)

OFFICIAL REFEREE.

There are three officers of the High Court who are known as Official Referees, and to them are allotted all those cases which involve the examination of accounts, or the long investigation of intricate matters which cannot be conveniently inquired into in open court. They are, in addition, the persons who occupy, in their public capacity,

a position similar to that of referees in an arbitration (*q.v.*). In respect of their powers, however, the Official Referees are greatly superior to the ordinary referees, as by statute their authority and jurisdiction are not much inferior to those of a High Court judge.

OLD STYLE.

The calendar, as used in Russia and the Balkan States, is thirteen days in arrear of that in use in the other civilised nations of the world. This is the "old style." The "new style," or Gregorian Calendar, was accepted by the majority of European countries in the sixteenth, and by Great Britain in the eighteenth century. The new style has, however, been adopted by Russia and the Balkan States, so far as the post office is concerned.

ONCOST.

(See COST ACCOUNTS, p. 352.)

ONEROUS PROPERTY.

It frequently happens in cases of bankruptcy that the property of the bankrupt is saddled with obligations of a more or less extensive character, and as the trustee in bankruptcy steps into the shoes of the debtor he is bound to accept the property with its burdens. This might frequently create great hardships and difficulties and prevent any person undertaking the position of a trustee. It is provided, however, by law that the trustee may, under certain specified conditions, disclaim all interest in such onerous property, and if he does so he is in no wise liable, nor is the bankrupt's estate further liable, for the same. In some cases it is necessary for the trustee to obtain the permission of the Court before he can disclaim; in others he is empowered to act upon his own responsibility.

OPEN ACCOUNT.

(a) An account which is not closed by settlement of the balance (*i.e.* one in regard to which an amount is owing which may be either not yet due or considerably outstanding).

(b) Any account in the books which is not balanced off.

(See also BALANCE SHEET, p. 136.)

OPEN COURT.

A court of justice to which the public are admitted, and the proceedings of which may be freely and fully reported, consistently with order and decency. A court can be cleared in exceptional cases, especially if the demeanour of the audience is improper. But it is only in rare instances that cases can be heard *in camera*, some of them being provided for by statute, and others depending upon the decision of the presiding judge. In civil actions many interlocutory applications are heard in chambers, that is, private

rooms set apart for the purpose, and to these no one has access except the parties to the case and their legal advisers.

OPENING ENTRIES.

When opening a new set of books or commencing a system of accounts, it is necessary to bring into account the assets and liabilities of the business. This is done by means of Journal entries, which are known as opening entries, and are made in the following form—

At the end of October, 19..., a firm's books showed the following balances: Overdraft at Bank, £10; Creditor, A. Morgan, £230; Debtors, C. Burnaby, £364, and D. Read, £84; Bills Payable, £125; Bills Receivable, £200; Goods, £1,124 10s. 0d.

JOURNAL. OPENING ENTRIES.

		£	s.	d.	£	s.	d.
Sundry Assets	Dr.						
To Sundry Liabilities	Cr.						
C. Burnaby	Dr.	364	0	0			
D. Read	Dr.	84	0	0			
Bills Receivable	Dr.	200	0	0			
Goods Account	Dr.	1,124	10	0			
To Bank	Cr.				10	0	0
" A. Morgan	Cr.				230	0	0
" Bills Payable	Cr.				125	0	0
" Capital Account	Cr.				1,407	10	0
		£1,772	10	0	£1,772	10	0

In Continental systems, as the books are absolutely closed at the end of each period, it is necessary to re-open them at the beginning of each period (*i.e.* the next day), when the opening entries are always passed through the Journal. (See also LIMITED COMPANY ACCOUNTS, p. 634.)

OPERATING COSTS.

(See COST ACCOUNTS, p. 346.)

ORGANISATION OF AN ACCOUNTANT'S OFFICE.

Time employed by principals and clerks is the "Stock in Trade" of the professional accountant. The value of the time employed depends upon experience and knowledge and skill in applying them to a variety of matters from day to day, so as to get the best possible results in the shortest possible time. Organisation of an accountant's office should, therefore, aim at—

(1) Making the best use of time employed.

(2) Keeping a full and correct record of the work done and the time employed upon it.

CLERKS.—To achieve the first object, a judicious mingling of skilled and partly skilled clerks enables matters to be carried out at the minimum cost. The managing clerks should be men of character able to employ less skilled or less intelligent clerks to assist them in carrying

out the lesser details. In the course of doing so the managing clerks will train those subordinates according to their respective capabilities, so that, if qualified, they may in time become managing clerks themselves. A large part of an accountant's business is carried on outside his own offices, in town or country or abroad, and on the ground of expense division of labour is not always possible or economical. There is, therefore, a limit to the grading of work and principals themselves, and more often managing clerks, must at times do their own detail work. Where an accountant has much work of a recurring nature to do at any given centre it is, therefore, economical to set up a branch or agency. In a large practice it is convenient to sub-divide not only skilled and less skilled work, but also the different classes of matters which come within an accountant's practice, including audits, investigations, devising and writing up books adapted to any and every undertaking, preparation of accounts of every kind, receiverships, liquidations, bankruptcies, secretarial work, income tax, business organisation, costing, etc. Expert book-keeping lies at the root of an accountant's training and the members of his staff should be thoroughly grounded in the art of writing up and balancing books quickly and expeditiously before being drafted to any other class of work. Experience in the several branches of accountancy all help to make sound auditors, for an auditor can never have too much general as well as special knowledge. After a general training a member of the permanent staff should be attached to one department, so that he may become a specialist in that department, able, under the principal's direction, to grasp new matters and handle them with the dispatch and certainty that comes of first-hand knowledge and experience. This sub-division is, however, only possible in a large practice. In a smaller practice the principal himself must manage each department personally and utilise his staff in one or the other as circumstances dictate. For this reason a large firm, properly organised, should be able to offer the more efficient and economical service, and make the best use of time employed.

TIME RECORDS.—The time records, which are the basis of an accountant's charges, are a matter of office routine. It is necessary to know when a principal or clerk arrives, when he goes out, where he goes, when he comes in again, and on what matter he is occupied, whether in the office or out of it. For this purpose a timekeeper, stationed at the entrance to the office, keeps a Daily Attendance Book, containing the names of each principal and each clerk, arranged in alphabetical order, in which he enters the necessary particulars in columnar form. The clerk, as he comes in, tells the timekeeper on what matter he is engaged.

If the principal or a clerk goes direct to a matter at a distance from the office, or is in the country or abroad, the place where he is occupied is entered in the Attendance Book. For the use of the principals, the timekeeper also prepares a List of Clerks, arranged in alphabetical order, in which he enters the name of the clerk, time of arrival, matter on which occupied, and where occupied, or whether unoccupied. This list is submitted to a partner first thing in the morning for scrutiny, and is handed to any partner who requires clerks to take up a matter.

DIARIES.—Each principal and clerk keeps a Diary in which he enters daily the name of the matter on which engaged, short particulars of the work done, the year or period to which it relates, and the time occupied. If engaged on office work not chargeable to a client, he enters up his Diary accordingly. If engaged away from the office he sends particulars daily, which are written up in his Diary by the charges clerk. The charges clerk is in charge of all the Diaries and it is his business to see that they are written up to date and in sufficient detail. Each principal and clerk (or the charges clerk for them) raises a monthly Summary of the time recorded in his Diary on a Summary Sheet with 27 columns, so that each day's time may be extended opposite the matter to which it relates. This furnishes the total time for the month chargeable to each matter. From the Summaries the total time for the month of each principal and clerk is posted to a Clients' Time Ledger, containing the clients' accounts, arranged in alphabetical order. This ledger is ruled with a number of columns (for hours only), the name of the principal or clerk is put at the top of the column and the time occupied entered below the respective names. The total principals' and clerks' time for the month charged to each client is added up in the Time Ledger and the totals entered in a Clients' Charges Journal. This journal is ruled with columns to take six months' time in hours and moneying out (the aggregate principals' and aggregate clerks' time being shown separately). At the beginning of every six months the name of every client is entered in the journal in alphabetical order to correspond with the Clients' Time Ledger, the monthly time being entered each month in the respective columns opposite the client's name and moneyed out. The total time for the month, as entered in the journal, is agreed with the aggregate total time appearing on the summaries referred to above. The monthly totals are posted to the Clients' Charges Ledger and the total credited to Charges Account. There is, therefore, a complete record of the time occupied on each matter and of the principals and clerks engaged thereon, and a comparison may be made of the time occupied from year to year. From the Clients'

Charges Ledger the bills are prepared and sent out as soon as a matter is completed. The time is charged out at a fixed rate for each principal and, in the case of a clerk, according to the rate of salary paid him, or at an average rate to cover salaries and expenses. It is only by seeing that, as far as possible, a clerk's time is spent on the class of work appropriate to his experience, knowledge, and capacity that charges can be kept within reasonable dimensions.

BILLS RENDERED BOOK.—It is the duty of the charges clerk to ascertain when a matter is completed and to draft the clients' bills for submission to the principal. The bills, when settled, should be typed with a carbon copy, the carbons being numbered and filed for reference in numerical order. The name of the client, amount of the charges, and date rendered should be written up in a Bills Rendered Book, with columns in which to enter date of payment and memoranda. From this book bills rendered and not paid can be readily ascertained.

AUDITS.—The tendency is for most clients to close their books at the end of the calendar year, thus causing considerable congestion in an accountant's office at one period of the year and possibly some slack time at another. During the slack time the staff should be preparing skeleton accounts and schedules for the ensuing audits. This effects a considerable saving of time during the busy period. The audit staff may also be drafted to other departments for the time being, but in a large practice only careful organisation can avoid a certain amount of time unoccupied at certain seasons of the year, that is, if a sufficient staff is kept to deal with audits with reasonable promptitude. In view of the nature of the work it is not expedient to employ temporary clerks, even for minor details, nor is a temporary clerk likely to have the necessary qualifications. To avoid overlapping and delay a complete list of audits should be made setting out in columnar form the name of the matter, the date on or about which the accounts are usually ready, the names of the principals and clerks employed on it, and the total time occupied from year to year. The clerks can then be allotted to the various audits in such a way as to avoid overlapping and consequent delay. One can also ascertain whether the audit is taking the same average time from year to year. An individual list should be prepared showing how many audits are undertaken by each clerk, and the time at which the audits usually have to be done. As soon as a managing clerk has been told off to a sufficient number of matters to keep him occupied throughout the year, nothing further should be added to his list, sufficient juniors being allotted to him to relieve him of purely detail work. As subordinates become sufficiently trained to be moved up, a managing

clerk is able to delegate the old and take up new matters.

Two notebooks should be kept for each audit: one a permanent notebook containing information likely to be required for reference from year to year; the other containing notes and queries arising on the current audit and the replies thereto.

With the exception of secretarial duties, the work in other departments being intermittent and non-recurring as regards individual matters, does not lend itself to organisation in the same way as audits. The work is taken up as it arises by a principal and his managing clerks and juniors and carried out according to circumstances.

FILING.—In an accountant's office there is inevitably an accumulation of papers relating to the various matters on which he is engaged. The papers relating to each matter should be kept in a separate bundle or a separate file. As the papers frequently have to be taken away from the office, bundles are, on the whole, a more convenient form in which to keep papers, each of which should be suitably endorsed. A number should be given to every matter and a corresponding number attached to the bundle. A Register of Papers should be kept. In the register each matter should be entered in alphabetical order with its corresponding number. The bundles should be put away in the order of the numbers. If a bundle is kept in a deed box a note is made in the register indicating where the box is kept.

In other respects the organisation of an accountant's office does not differ from that of any other office.

OUTPUT.

The total quantity or value of goods manufactured during a period. (See also **COST ACCOUNTS**, p. 346.)

OUTSTANDING ACCOUNTS.

Accounts remaining unpaid beyond the time at which payment is due.

At the close of each financial period the outstanding accounts receivable should be listed in a schedule prepared by extracting the debit balances from the personal ledger accounts.

The list of outstanding debts should be subjected to a very critical examination by the auditor. The composition of each debt should be verified (*i.e.* the detailed deliveries of which it is composed should be traced), and in cases in which the composition of the account is not clear, explanations should be sought from reliable sources. The age of the debt, the terms of credit, the regularity or otherwise of previous settlements should all be noted with a view to deciding whether the debt is good. A list of questionable debts should be prepared, and each account represented should be gone into with a responsible official, and proper

charges and reserves made in respect of bad and doubtful debts.

A commendable procedure is that of circularising debtors with a request that any discrepancy in the statement rendered should be communicated to the auditors. Where this system is adopted the circulars may be made out by the office staff; but they must be checked by the auditor who must also dispatch them.

OUTSTANDING LIABILITIES AND PAYMENTS IN ADVANCE.

(See ADJUSTMENTS AT BALANCING TIME;
INVESTIGATIONS, p. 576.)

OUTWARDS CONSIGNMENT.

(See CONSIGNMENT ACCOUNTS.)

OVERDUE ACCOUNTS, LOANS.

Outstanding accounts which are overdue should be subject to careful examination by the auditor in order to determine, in the first place, the extent to which they may be regarded as good, and, in the second place, to satisfy himself that they have not actually been paid and the sums received misappropriated. Probably the best means of proof available to the auditor in this matter is that of sending out to each of the debtors a statement of his accounts prepared by the office staff, checked and dispatched by the auditor, asking him to communicate direct with the auditor in the event of any discrepancy or error being found in the statement. This method will probably lead to the disclosure of fraud, if it has been committed, and will, at the same time, reveal the existence of disputes and claims in connection with the accounts which might otherwise not come to the notice of the auditor, and in respect of which he will naturally require proper reserves to be made.

This system of circularising is very applicable to the case of loans. Sometimes the circular takes

the form of a printed statement showing the number of the loan holder's pass book and the amount standing to his credit, with a request to the loan holder to compare the statement with his loan pass book.

Where pass books are issued for loans, the auditor should see that they are numbered consecutively and should keep a record of those issued. When loans are repaid the loan book should be retained, duly cancelled, and produced as additional evidence of repayment to the auditor, who should at the same time require proof that the books unissued are still on hand.

An additional precaution may be taken by arranging that a statement showing the amount deposited, and the total amount of the loans advanced by the depositor, which has been checked, signed and dispatched by a director, shall be sent to every loan holder as each deposit is made.

OVERHEAD CHARGES.

(See COST ACCOUNTS, p. 345; ESTABLISHMENT EXPENSES.)

OVER-RIDING COMMISSION.

(See UNDERWRITERS' ACCOUNTS.)

OVERT ACT.

An open or manifest act, which can be manifestly, and not merely inferentially, proved. It is to be noticed that in charges of treason, either one overt act must be proved by at least two distinct witnesses, or two overt acts of the same character by one witness to each.

OVERTRADING.

Trading beyond the capacity of the capital employed in the business, with the result that, owing to the locking-up of same in stock and book debts, it is difficult or impossible to meet the claims of creditors.

PACKAGES CHARGED FOR BUT CREDITED WHEN RETURNED.

THERE are several methods of dealing with items of this nature in the books of account. The method most commonly adopted in practice is to provide a separate column in the Day Book and Ledger, in which the value of packages charged out are recorded. They are thus kept separate from the actual sales in the Day Book, and may be posted in total to a "Packages charged" Account. An extra column will be necessary on each side of the Ledger. On the debit side, the packages charged will be debited from the Sales Day Book, and on the credit side those returned will be posted from the Returns Inwards Book. There will thus be distinct records in each Ledger Account of the packages and of sales. The balances on the "packages" columns will form a record of outstanding packages.

As packages are frequently charged out at prices which include a profit, and which in the event of their being returned will not be realised, it will be the duty of the auditor to see that a proper reserve is made to cover the excess over cost of packages remaining in the hands of customers at stocktaking.

This system of recording packages is sometimes varied or supplemented by a statistical record in ledger form, in which customers are debited with the quantities (and values) of packages sent out, and credited with returns (*e.g.* Cask Ledgers and Bottle Ledgers in brewery concerns).

PACKING MATERIAL.

When the cost of packing material is included in the sales as an extra charge, the cost of the material used should be charged against the Trading Account. If the packing is supplied free and is not returnable, it may be regarded as an expense of distribution, and, as such, forms a charge against Profit and Loss Account.

In cases in which the raw timber is purchased and converted into cases by the employees of the firm, the value of the timber used and the wages of employees engaged in making the cases should be charged to the Packing Material Account.

In some businesses it is the practice to capitalise the original cost of packing cases, renewals and repairs being charged to revenue. This is a doubtful proceeding, because, unless a very strict record is kept of the cases, there is a great danger of lost and damaged cases not being replaced, and consequently there is an over-valuation of the asset in the Balance Sheet.

PAID-UP CAPITAL.

This refers to that portion of a company's capital which has been called up and upon which payment has been received by the company. It is represented by the amount of cash actually received on the shares issued, together with the value of the shares allotted as paid up for a consideration other than cash.

PARITY.

The equivalent in London, for example, of a price quoted, say in New York or any other country arbitrage (*e.g.* an American stock is quoted in New York at 75, and the current telegraphic transfer rate is 4.86). The equivalent or parity price in London would be—

$$\frac{75 \times 20/-}{4.86 \times 4/-} = \frac{1500}{19.44} = 77.16$$

On the other hand, supposing the quotation in London to be 77.16, the corresponding value in New York may be obtained, among other ways, by the following—

$$\text{London price } \frac{77.16}{1/10} \times (4.86 \times 2) = \frac{1500}{7.716} = 74.99, \text{ or } 75.$$

PART PAYMENT.

Any sum of money which is paid by a debtor to his creditor in connection with an account or transaction existing between them. Thus, if A purchases goods from B of the value of £10 or upwards, and on the making of the contract A pays a sum of £5 to B, as a part of the price of the goods, this is part payment, and the fact of this payment is sufficient to take the case out of Section 4 of the Sale of Goods Act, 1893, which requires, when there is an executory contract of sale of goods of the value of £10 or upwards, that the purchaser shall give to the seller something by way of earnest or of part payment in order to make the contract enforceable, unless the contract is evidenced by some note or memorandum in writing. The question of part payment is important in respect of debts of long standing in order to prevent the Statute of Limitations (*q.v.*) running; for if such part payment is made, the period within which the creditor can sue, six years or twenty years, according as the contract is a simple one or a specialty one, dates from the time of such part payment (or the last of such part payments, if there are more than one) and not from the date of the contract. It would appear

that a statute-barred debt is not revived by any such part payment if the debt has already become barred by lapse of time when the part payment is made. Part payment by one co-contractor or co-debtor does not keep alive the debt as against the other or others.

PARTLY-SECURED CREDITORS.

(See *BALANCE SHEET*, p. 137; *BANKRUPTCY ACCOUNTS*, p. 163.)

PARTNERS.

(See *PARTNERSHIP ACCOUNTS*.)

PARTNERS, SLEEPING.

(See *AUDITING*, p. 112.)

PARTNERSHIP ACCOUNTS.

Partnerships are governed by the provisions contained in the Partnership Act, 1890, and in the Limited Partnerships Act, 1907, and also by the rules of equity and of common law applicable to partnerships, except so far as they are inconsistent with the express provisions of those Acts. (Sec. 46 P.A. 1890 and Sec. 7 L.P.A. 1907.)

The Partnership Act, 1890, merely codified the then existing law, whilst the Limited Partnerships Act, 1907, introduced into English partnership law the principle of limited liability in partnerships which, until then, had not been recognised in this country, though it has long been in force in some European countries and in the United States.

Section 1 of the Companies (Consolidation) Act, 1908, limits the number of persons who can carry on business without registering as partners to twenty, except in the case of a banking business, when the number must not exceed ten.

We may, therefore, consider partnerships as divided into two classes, ordinary partnerships, where the liability of all the partners is unlimited, and limited partnerships, where the liability of one or more partners is limited, and the liability of one or more is unlimited. For the purpose of dealing with Partnership Accounts, it will, however, be sufficient to deal with ordinary partnerships only, preceded by a few supplementary remarks as to the special features of a limited partnership.

DEFINITION.—A partnership is defined by Section 1 of the Partnership Act, 1890, as "The relation which subsists between persons carrying on a business in common with a view of profit," but this definition is not absolutely conclusive, and Section 2 of the Act lays down certain rules for determining whether a partnership does or does not exist.

The term "business" is defined by Section 45 as including every trade, occupation or profession, but this too, appears subject to qualification, particularly as regards persons who are engaged in an occupation in contradistinction to a business, as in the cases of joint ownership, tenancy in

common, and the like, for example:—A and B are joint owners of a house, which they let, sharing the rent after paying thereout for repairs and other outgoings. A and B are not partners.

C and D are tenants-in-common of certain leasehold property which they sublet, and after payment of expenses, share the balance of profit rental. C and D are not partners.

Under the Partnership Act, 1890, the liability of the partners is unlimited and this applies whether partners are active partners or merely dormant or sleeping partners, and under the provisions of Section 14 of the Act, it is quite possible for a third party to render himself liable as a partner in a firm of which he is not a partner, by representing himself, or knowingly suffering himself to be represented as such to anyone who has, on the faith of any such representation, given credit to the firm. This is known as "holding out," and is a special application of the principle of estoppel.

Ordinary partnerships are governed chiefly by the Partnership Act, 1890, subject to modification of the provisions of the Act by mutual agreement between the partners. This agreement need not necessarily be in writing, it may be a parol agreement, or it may even be inferred from the course of dealing of the partners. For example: If it is found on examination of the books of the partnership, that the partners have been in the habit of dividing profits in certain proportions, this will be taken as evidence of an agreement to that effect.

However, from a practical point of view there is no question but that a Partnership Deed, fixing the terms of the partnership, is always to be desired.

One peculiarity of partnership is, that as between the partners the relation of principal and agent exists in a dual aspect, each partner being principal as far as he himself is concerned, and at the same time agent as far as his partners are concerned, in respect of any act done by him in the ordinary and proper conduct of the business of the firm.

As between a partner and his co-partners there may be limitations to his authority to act for the firm, but this does not affect his power to bind the firm so far as third parties are concerned, unless they had notice of such limitation, or did not know or believe him to be a partner.

Under these circumstances, therefore, the first thing to be done in dealing with Partnership Accounts is to ascertain exactly the terms of the agreement between the partners. If these are contained in the Deed, an abstract of its provisions should be made for reference, showing particularly those provisions which affect the accounts.

As regard the provisions of the Partnership Act, 1890, the principal points relating to accounts

are contained in the following subsections of Section 24—

(1) All the partners are entitled to share equally in the capital and profits of the business and must contribute equally towards losses whether of capital or otherwise sustained by the firm. . . .

(3) A partner making, for the purpose of the partnership, any actual payment or advance beyond the amount of capital which he has agreed to subscribe, is entitled to interest at the rate of 5 per cent. per annum from the date of the payment or advance.

(4) A partner is not entitled, before the ascertainment of profits, to interest on the capital subscribed by him. . . .

(6) No partner shall be entitled to remuneration for acting in the partnership business.

Where there is a Partnership Deed, the above provisions are, as a rule, varied to a greater or less extent.

The following are the chief points in relation to the accounts as to which it is desirable that the Partnership Deed should contain express provision.

(1) As to capital. The amount to be contributed by each partner should be stated, and whether or not the capitals are to be fixed.

(2) As to the division of profits and losses between the partners, including particularly the following points—

(a) Partners' Salaries (if any).

(b) Interest on Capital.

(c) Interest on Drawings.

(d) Interest on Current Accounts (if any).

(e) Division of net profit.

(3) As to the amount which each partner shall be entitled to draw from time to time in advance of profits.

(4) As to books of account. Proper books of account should be kept to which all partners are entitled to have access, and at stated periods a Trading and Profit and Loss Account should be prepared showing the amount divisible amongst the partners, and a Balance Sheet should be drawn up at the end of each period, which Balance Sheet having been agreed to and signed by each of the partners will be binding on all, subject to the correction of manifest errors discovered within a specified time. Provision should also be made for the proper audit of the accounts.

(5) As to the method of arriving at the amount of goodwill in the event of the death, or retirement, of any partner.

(6) As to the dissolution of the partnership. In order to avoid dissolution of the partnership in the event of the death, bankruptcy or retirement of a partner, it is desirable that some provision be made, whereby such deceased, bankrupt or retiring partner's share can be ascertained either by providing that accounts shall be taken at the date of his death, bankruptcy or retirement,

and his share in the business ascertained up to that date, or, if it is desired to avoid the trouble and expense of stock-taking, by providing that the capital of the deceased, bankrupt or retiring partner shall be taken to be the sum at which it appears in the last signed Balance Sheet plus interest to the date of his death, bankruptcy, or retirement at a certain rate per cent. per annum in lieu of profits.

(7) As to the requirements of the share of a retiring partner by the survivor. Provision should be made for the share of a deceased, bankrupt or retiring partner to be acquired by the surviving partner on terms, particularly as regards the payment thereof by instalments.

(8) As to the duration of the partnership. This should be fixed, otherwise the partnership will be a partnership at will and can be determined by any partner giving notice to the other partner or partners to terminate the partnership at any time.

(1) **INTEREST ON CAPITAL.** This can only be charged where there is a specific agreement to that effect.

The object of charging interest on capital, is to ascertain whether the profits after charging interest are sufficient to warrant the continuance of the business, considering that the liability of the partners is unlimited, and further, to enable the rights of the partners *inter se* to be properly adjusted as regards capital.

In those cases where the capitals are fixed, and the profits are shared in proportion to capital, the ultimate result to the partners is the same whether interest is charged or not, but even in these cases, it is advisable to charge interest for the first named reason.

In other cases, the result will be as follows—

(a) Where capitals are equal, but profits are shared in different proportions, the partner entitled to the greater share of profits will benefit if interest be not charged.

(b) If the capitals be unequal, but the partners share profits equally, then the partner with the larger capital will, under similar circumstances, lose.

(c) Where the capitals are unequal, and the profits are shared unequally, the result to each partner depends upon the proportion which respective capitals bear to one another as compared with the proportions in which the profits are shared. In such cases, the partner whose proportion of capital is greater than his proportion of profits will benefit by the charging of interest on capital.

This is easily seen by the following examples, the rate of interest on capital being taken at 5 per cent.—

(A) *Capitals equal.—Profits shared unequally.*

A and B are partners, and their capitals are fixed at £1,000 each. They share profits in proportion—A $\frac{2}{3}$ rds, B $\frac{1}{3}$ rd. The profits for the year are £1,000. If interest be not charged, A's share of

the profits will be £667, and B's £333. If interest on capital be charged, then each will be entitled to £50 interest on capital. This will leave £900 to divide, of which A will be entitled to £600, and B to £300, making the total amount received by each as follows: A £650, B £350. Thus in this case, A being entitled to the larger share of profits, will benefit if interest on capital be not charged.

(B) *Capitals unequal—Profits shared equally.*

A's capital £1,500. B's capital £500. Profits shared equally. Profit for the year, £1,000. If no interest on capital is charged, A takes £500 and B £500. If interest on capital be charged, A will be entitled to £75 interest, and B £25 interest, leaving £900 to divide equally between them. Thus A will receive £75 interest and £450 profit, making £525, and B will receive £25 interest, and £450 profit, making £475, so that in this case, if interest on capital be not charged, A being the partner with the larger capital, will lose.

(C) *Capitals unequal—Profits shared unequally.*

A's capital £2,000. B's capital £1,000. Profits shared—A $\frac{2}{3}$ ths, B $\frac{1}{3}$ ths. Profit for the year £1,000. In this case A's proportion of the capital is $\frac{2}{3}$ rd to B's $\frac{1}{3}$ rd; this is greater than A's share of the profits, which is only $\frac{2}{3}$ ths. Therefore, A will benefit by the charging of interest on capital as follows: If interest be not charged, the shares of profits will be—A $\frac{2}{3}$ ths = £600, B $\frac{1}{3}$ ths = £400. If interest on capital be charged, then A will be entitled to £100 and B to £50, leaving £850 to divide as profit, of which A will be entitled to $\frac{2}{3}$ ths = £510, and B to $\frac{1}{3}$ ths = £340. Thus A will receive in all £610, and B £390. A, therefore, benefits by the charging of interest on capital.

(2) **INTEREST ON DRAWINGS.**—If the partners' drawings are irregular, it is advisable that interest should be charged thereon, so that the rights of the partners may be accurately adjusted.

Where the capitals are fixed and current accounts are kept, interest should be credited and debited on the items appearing in the current accounts.

(3) **PARTNERS' SALARIES.**—Under the provisions of the Partnership Act, no partner is entitled to remuneration for acting in the partnership business, but it is very usual to vary this provision by providing for payment of fixed salaries to one or more, or all of the partners, and for this there are various reasons—

(a) In order that the business may be charged with a proper amount commensurate with the services rendered by the partners respectively to the firm.

(b) In cases where one or more of the partners leave the conduct of the business in the hands of another partner or partners.

(c) Where the capital is contributed by one or more partners, but the practical knowledge

necessary is supplied by another partner or partners, who possibly have not invested the same amount of capital in the business.

(d) In cases where junior partners have been taken into a business, it is very usual to provide that they should be paid a fixed salary, and have in addition, only a small proportion of the profits of the business.

As regards the book-keeping in the case of a partnership, this differs in no respect from that of a single trader, except that separate accounts will have to be opened for the capital and drawings of the partners, and the balance of profit will have to be apportioned between them.

EXAMPLE No. 1

A, B, and C carry on business in partnership as Engineers.

The following was the Trial Balance on 31st December, 19..—

	£	s.	d.	£	s.	d.
Stock, 31st December, 19..	2,800	0	0			
Purchases	12,600	0	0			
Wages and Expenses	3,700	0	0			
Sales				22,000	0	0
Salaries	800	0	0			
Rent, Rates and Taxes	500	0	0			
Fuel and Light	150	0	0			
Insurance, Fire and Workmen's Compensation	190	0	0			
Office Expenses	220	0	0			
Discounts	250	0	0			
Bank Interest and Commission	20	0	0			
Partners' Salaries	1,000	0	0			
A. Drawing Account—						
Balance, 31st Dec., 19..				300	0	0
" Drawing during 19..	400	0	0			
B. " Balance, 31st Dec., 19..				120	0	0
B. " No Drawings						
C. " Balance, 31st Dec., 19..				400	0	0
C. " Drawings during 19..	200	0	0			
Life Insurance Premium	35	0	0			
Life Policy Surrender Value, 31st Dec., 19..	300	0	0			
Office Furniture	150	0	0			
Sundry Debtors	4,000	0	0			
Cash at Bank	230	0	0			
Cash in hand	25	0	0			
Sundry Creditors				1,925	0	0
Bills Payable				825	0	0
C. Loan Account (@ 5 %)				500	0	0
A. Capital Account				500	0	0
B. " "				500	0	0
C. " "				500	0	0
	£ 27,570	0	0	£ 27,570	0	0

Stock on hand 31st December, 19..—£3,050.

Surrender value of Life Policy on 31st December, 19..—£325.

Interest on drawings at 5 per cent. per annum. The average date of the drawings during the year was 30th June.

Interest on capital at 5 per cent. per annum. The profits were divided—A $\frac{2}{3}$ ths, B $\frac{1}{3}$ ths. C $\frac{1}{3}$ ths.

The closing entries will be as follows—

MESSRS. A, B & C.—ENGINEERS

Dr. TRADING AND PROFIT AND LOSS ACCOUNT FOR THE YEAR ENDED 31ST DECEMBER, 19.. Cr.

		£	s.	d.	£	s.	d.		£	s.	d.	£	s.	d.
19..	To Stock at date	2,800	0	0				19..	By Sales . . .			22,000	0	0
Dec. 31								Dec. 31						
19..	„ Purchases .	12,600	0	0										
Dec. 31														
	Less Stock, 31st Dec., 19.. .	15,400	0	0										
		3,050	0	0										
	To Wages and Expenses .				12,350	0	0							
	„ Gross Profit—carried down				3,700	0	0							
					5,950	0	0							
					£22,000	0	0					£22,000	0	0
19..	To Salaries .				800	0	0	19..	By Gross Profit—brought down			5,950	0	0
Dec. 31	„ Rent, Rates and Taxes .				500	0	0	Dec. 31						
	„ Fuel and Light				150	0	0							
	„ Fire and Workmen's Compensation Insurance .				190	0	0							
	„ Office Expenses				220	0	0							
	„ Discounts .				250	0	0							
	„ Bank Interest and Commission .				20	0	0							
	„ Balance carried down . .				3,820	0	0							
					£5,950	0	0					£5,950	0	0
19..	To Partners' Salaries .				1,000	0	0	19..	By Balance brought down			3,820	0	0
Dec. 31	„ Interest on Capital, Drawings and Loan				126	0	0	Dec. 31						
	„ Life Assurance Premium—Balance				10	0	0							
	„ Profit—													
	A. 7/20ths	939	8	0										
	B. 6/20ths	805	4	0										
	C. 7/20ths	939	8	0										
					2,684	0	0							
					£3,820	0	0					£3,820	0	0

A, B & C

A.—DRAWING ACCOUNT

Dr.				Cr.			
19..		£	s. d.	19..		£	s. d.
Dec. 31	To Sundries . . .	400	0 0	Dec. 31	By Balance . . .	300	0 0
	„ Balance carried down . . .	869	8 0	19..			
				Dec. 31	„ Interest on Capital and Drawings . . .	30	0 0
					„ Profit and Loss Account—Share of Profit, 7/20ths . . .	939	8 0
		<u>£1,269</u>	<u>8 0</u>			<u>£1,269</u>	<u>8 0</u>
				19..			
				Dec. 31	By Balance brought down . . .	869	8 0

B.—DRAWING ACCOUNT

19..		£	s. d.	19..		£	s. d.
Dec. 31	To Balance carried down . . .	956	4 0	Dec. 31	By Balance . . .	120	0 0
				19..			
				Dec. 31	„ Interest on Capital and Drawings . . .	31	0 0
					„ Profit and Loss Account—Share of Profits, 6/20ths . . .	805	4 0
		<u>£956</u>	<u>4 0</u>			<u>956</u>	<u>4 0</u>
				19..			
				Dec. 31	By Balance brought down . . .	956	4 0

C.—DRAWING ACCOUNT

19..		£	s. d.	19..		£	s. d.
Dec. 31	To Sundries . . .	200	0 0	Dec. 31	By Balance . . .	400	0 0
	„ Balance carried down . . .	1,204	8 0	19..			
				Dec. 31	„ Interest on Capital, Loan & Drawings . . .	65	0 0
					„ Profit and Loss Account—Share of Profit, 7/20th . . .	939	8 0
		<u>£1,404</u>	<u>8 0</u>			<u>£1,404</u>	<u>8 0</u>
				19..			
				Dec. 31	By Balance brought down . . .	1,204	8 0

A, B & C

LIFE POLICY ACCOUNT

19..		£	s. d.	19..		£	s. d.
Dec. 31	To Surrender Value at date . . .	300	0 0	Dec. 31	By Balance carried down—Surrender Value at date . . .	325	0 0
19..							
Dec. 31	„ Life Insurance Premium Account . . .	25	0 0				
		<u>£325</u>	<u>0 0</u>			<u>£325</u>	<u>0 0</u>
19..							
Dec. 31	To Balance brought down—Surrender Value at date . . .	325	0 0				

Dr.				LIFE INSURANCE PREMIUM ACCOUNT								Cr.			
19..				£				s.				d.			
Dec. 31				35				0				0			
To Cash—Premium															

MESSRS. A, B & C.—ENGINEERS

BALANCE SHEET. 31ST DECEMBER

<i>Liabilities.</i>								<i>Assets.</i>					
Sundry Creditors .	£	s.	d.	£	s.	d.		£	s.	d.	£	s.	d.
Bills Payable .	1,925	0	0					Office Furniture .			150	0	0
	825	0	0					Life Policy .			325	0	0
C. Loan Account .				2,750	0	0		Stock .			3,050	0	0
Capital Accounts—A	500	0	0	500	0	0		Sundry Debtors .			4,000	0	0
B	500	0	0					Cash at Bank .	230	0	0		
C	500	0	0					Cash in hand .	25	0	0		
Drawing Accounts—A				1,500	0	0					255	0	0
B	869	8	0										
C	956	4	0										
	1,204	8	0										
				3,030	0	0							
				£7,780	0	0					£7,780	0	0

In some cases, accounts are kept only by single entry. The following is an example—

On the 1st January, 19.., A took B into partnership. A's books were kept by single entry and the firm's books continued to be so kept, A's Balance Sheet at 31st December, 19.., was as follows—

<i>LIABILITIES.</i>			<i>ASSETS.</i>		
	£	s. d.		£	s. d.
Sundry Creditors .	2,000	0 0	Fixtures & Fittings	500	0 0
A's Capital .	2,500	0 0	Stock-in-Trade .	1,000	0 0
			Sundry Debtors .	2,500	0 0
			Bills Receivable .	300	0 0
			Cash at Bank and		
			in hand .	200	0 0
	£4,500	0 0		£4,500	0 0

The partners were to receive 5 per cent. interest on their capitals, and profits or losses were to be divided—A two-thirds, B one-third.

It was agreed that B should not draw on account of profits more than £250 per annum (exclusive of interest on capital) until he had paid to A a premium of £500 out of his share of profits in excess of £250. Amounts due from B to A in respect of premium were to be transferred from his Capital Account to A's Capital Account. A's capital was to be £2,500 as shown by his

Balance Sheet at 31st December, 19... B's capital was to be £500, which he paid into the firm's Banking Account on 1st January, 19...

On 1st January, 19.., the firm's Balance Sheet was as follows—

<i>LIABILITIES.</i>			<i>ASSETS.</i>		
	£	s. d.		£	s. d.
Creditors .	2,000	0 0	Sundry Assets as		
Capital—A .	2,500	0 0	above (excluding		
B .	500	0 0	cash) .	4,300	0 0
			Cash in hand and		
			at bank .	700	0 0
	£5,000	0 0		£5,000	0 0

During the year A drew out an account of profits £600 and B £250.

At the 31st December, 19.., the sundry creditors amounted to £1,750, and the assets were as follows—

	£	s.	d.
Fixtures and Fittings	500	0	0
Stock-in-Trade .	1,200	0	0
Sundry Debtors .	2,700	0	0
Bills Receivable .	200	0	0
Cash .	300	0	0
	£4,900	0	0

This shows a difference at the end of the year

between the assets and liabilities of £3,150, which represents the joint capitals of A and B.

STATEMENT SHOWING GROSS PROFIT FOR THE YEAR.

	£	s.	d.
Excess of Assets over Liabilities, 31st Dec., 19..	3,150	0	0
Add Partners' drawings during Year	A. 600 B. 250		
	850	0	0
	4,000	0	0
Deduct Capital, 1st Jan., 19..	A. 2,500 B. 500		
	3,000	0	0
Gross Profit for the year	£1,000	0	0

The Profit and Loss Account will be as follows—

	£	s.	d.
5 % Deprn. Fixtures	25	0	0
Interest on Capitals:			
A. 5% on £2,500—125			
B. 5% on 500—25			
	150	0	0
Share of Profits:			
A. 1/3rd of £825—550			
B. 1/3rd of £825—275			
	825	0	0
	£1,000	0	0

Gross Profit . . . £1,000 0 0

The Partners' Capital Accounts will then be as follows—

Dr.				A.—CAPITAL ACCOUNT				Cr.							
19.. Dec. 31				To Drawings £ 600 0 0 „ Balance carried down 2,600 0 0				19.. Jan. 1				By Capital £ 2,500 0 0 „ Interest on Capital 125 0 0 „ Share of Profit 550 0 0 „ Transfer from B on a/c of premium 25 0 0			
				<hr/> <div>£3,200 0 0</div> <hr/>								<hr/> <div>£3,200 0 0</div> <hr/>			
								19.. Dec. 31				By Balance brought down 2,600 0 0			

B.—CAPITAL ACCOUNT

19.. Dec. 31	To Drawings	£	s.	d.	19.. Jan. 1	By Capital	£	s.	d.
	„ A. Capital A/c transfer	250	0	0	Dec. 31	„ Interest on Capital . .	500	0	0
	of shares of profits in					„ Share of Profits	25	0	0
	excess of £250	25	0	0			275	0	0
	„ Balance carried down .	525	0	0					
		<u>£800</u>	<u>0</u>	<u>0</u>			<u>£800</u>	<u>0</u>	<u>0</u>
					19.. Dec. 31	By Balance brought down	525	0	0

and the Balance Sheet of the firm will appear thus—

A & B

BALANCE SHEET, 31st DECEMBER, 19..

Liabilities.	£	s.	d.	Assets.	£	s.	d.
Sundry Creditors	1,750	0	0	Fixtures	£500		
Capital Accounts—				Less Depreciation	25		
A. 2,600					475	0	0
B. 525	3,125	0	0	Stock-in-Trade	1,200	0	0
				Sundry Debtors	2,700	0	0
				Bills Receivable	200	0	0
				Cash	300	0	0
	£4,875	0	0		£4,875	0	0

GOODWILL IN PARTNERSHIP ACCOUNTS.—Goodwill has been variously defined. Lord Eldon defined it as "the probability that the old customers will resort to the old place." Lord Justice Lindley defined it as "the benefit arising from connection and reputation."

A consideration of this subject will show that there are several distinct ways in which goodwill may arise, as for instance—

(1) **From the reputation of the business.** In this case the goodwill arises from the right which the owner has to represent himself as the proprietor of such business.

(2) **From the situation of the business premises.** In this case the goodwill arises from the probability of customers resorting to the premises in which the business is being carried on.

(3) **From business connection.** Goodwill in this case consists in the right to be properly introduced to those having business relations with the concern.

(4) **From the personal reputation of the owner.** In cases where goodwill is based mainly upon personal reputation which cannot be separated from the individual, goodwill is practically non-existent. The value of goodwill varies considerably. It is usually calculated at so many years' purchase (generally $1\frac{1}{2}$ to 3) of the profits of the business based on the average profits for a number of years (generally 3 to 5).

GOODWILL IN THE CASE OF AN IN-COMING PARTNER.—Goodwill in a case of an in-coming partner may be treated in various ways, for example—

(1) It may be arranged that a certain sum shall be credited to the capital accounts of the old partners as representing goodwill, in which case a Goodwill Account must be debited with the amount, and the partners Capital Accounts credited in proportion as they share profits or losses, or as may be agreed. The capital brought in by the new partner, will be credited to his Capital Account. The advantage to the old partners lies in their respective capitals being increased by the amount of goodwill thus credited, and also by additional interest where interest is chargeable.

(2) It may be agreed that the in-coming partner shall pay to the old partners, a certain amount for goodwill, and shall, in addition, introduce a certain amount of capital. In this case, the amount paid for goodwill need not go through the books of the firm, but may be paid direct to the old partners. If passed through the firm's books, it will merely be credited to the old partners on receipt, and debited to them on the amount being paid out to them.

The Capital Accounts of the old partners will remain at the same figure, and the Capital Account

of the new partner will be the amount agreed to be paid in by him as capital.

(3) It may be agreed that the amount paid by the in-coming partner for goodwill, shall be left in the business as additional working capital, in which case the old partners' accounts will be credited with their due proportions (as in example 1) of the amount paid by the in-coming partner for goodwill.

In the latter two cases, it will be seen that no account will appear in the partnership books representing the asset of goodwill.

EXAMPLE 1

A and B carry on business in partnership and share profits or losses in proportion of A $\frac{3}{5}$ ths and B $\frac{2}{5}$ ths. Their capitals are A £6,000, B £3,000. They agree to take C into partnership on the 1st January, 19.., on the following terms—A and B are to be credited with goodwill £1,000 in the proportions in which they share profits. C is to bring in £2,000 as capital, and the profits are to be divided—A $\frac{3}{5}$ ths, B $\frac{2}{5}$ ths, and C $\frac{1}{5}$ th.

The books of the new partnership will be opened by journalising the assets and liabilities, including capital as shown by the Balance Sheet of the old firm on the date when the business is taken over by the new firm.

The following Journal entry will also be made—

19..		£	s.	d.	£	s.	d.
Jan. 1	Goodwill Account, Dr. To Sundry Accounts— A. Capital Account B. " " being $\frac{3}{5}$ ths to A, and $\frac{2}{5}$ ths to B, in accordance with the Agreement	1,000	0	0	600	0	0
					400	0	0

C pays into the Banking Account of the firm £2,000 which will appear in the Cash Book, and be posted to his Capital Account. The Capital Accounts of the partners will then appear as follows—

A.—CAPITAL ACCOUNT

19..		£	s.	d.
Jan. 1	By Capital in Old Firm . . .	6,000	0	0
	„ Goodwill . . .	600	0	0

B.—CAPITAL ACCOUNT

19..		£	s.	d.
Jan. 1	By Capital in Old Firm . . .	3,000	0	0
	„ Goodwill . . .	400	0	0

C.—CAPITAL ACCOUNT

19..		£	s.	d.
Jan. 1	By Cash . . .	2,000	0	0

EXAMPLE 2

A and B agree to admit C into partnership on the 1st January, 19.., on the terms that he pays to them £1,000 for goodwill, to be divided between them equally, and in addition brings into the firm the sum of £2,000 as capital.

In this case C will pay £500 each to A and B personally, which amount need not pass through the books of the firm.

If, however, it is preferred to preserve a record of the transaction in the books of the firm, the £1,000 received from C for goodwill, will be debited in the firm's Cash Book, and posted to the credit of A and B's Goodwill Account. The cash will then be paid out to A and B—£500 each—and these amounts will be posted to the debit of their Goodwill Account, the account thereby being closed.

A & B.—GOODWILL ACCOUNT.

19..		£	s.	d.	19..		£	s.	d.
Jan. 1	To Cash to A	500	0	0	Jan. 1	By Cash from C	1,000	0	0
	" " B	500	0	0					
		1,000	0	0			1,000	0	0

A record of the transaction will thus be shown in the books of the firm.

EXAMPLE 3

A and B take C into partnership on the 1st January, 19.., as in previous example, but it is agreed that £1,000 paid to A and B for goodwill, shall be left in the business. In this case, the amount paid in by C for goodwill, will be credited to the Capital Accounts of A and B in equal proportions. Assuming that their capitals in the old firm are £6,000 and £3,000 respectively, these accounts will then appear as follows—

A.—CAPITAL ACCOUNT

19..		£	s.	d.
Jan. 1	By Capital in Old Firm	6,000	0	0
	" Cash from C for Goodwill	500	0	0

B.—CAPITAL ACCOUNT

19..		£	s.	d.
Jan. 1	By Capital in Old Firm	3,000	0	0
	" Cash from C for Goodwill	500	0	0

C.—CAPITAL ACCOUNT

19..		£	s.	d.
Jan. 1	By Cash	2,000	0	0

Section 40 of the Partnership Act, 1890, provides that "where one partner has paid a premium to another on entering into partnership for a fixed

term, and the partnership is dissolved before the expiration of that term otherwise than by death of a partner, the Court may order the repayment of the premium, or of such part thereof as it thinks just, having regard to the length of time during which the partnership has continued, unless

(a) The dissolution is, in the judgment of the Court, wholly or chiefly due to the misconduct of the partner who paid the premium; or

(b) The partnership has been dissolved by an agreement containing no provision for the return of any part of the premium. It will be seen that the amount to be returned is wholly in the discretion of the Court, but as a general rule, following the judgment in *Attwood v. Maude* (L.R. 3 Ch. 369 (1868)), it will, in the absence of special reasons to the contrary, be an apportioned part of the premium based on the proportion which the unexpired part of the partnership term bears to the whole term.

GOODWILL IN THE CASE OF AN OUTGOING PARTNER.—In the case of a partner dying or retiring, the goodwill will have to be determined, either according to the terms of the Partnership Deed, or by valuation, and the Capital Account of the deceased or retiring partner, credited with his proportion thereof, and Goodwill Account debited therewith.

EXAMPLE 4

A, B and C carry on business in partnership. The Balance Sheet of the firm on the 31st December, 19.., was as follows—

LIABILITIES.					ASSETS.				
	£	s.	d.		£	s.	d.		
Sundry Creditors	1,500	0	0	Plant and Machinery	1,000	0	0		
Bills Payable	200	0	0	Loose Plant and Tools	800	0	0		
Capital—A	3,000	0	0	Stock	1,600	0	0		
B	2,000	0	0	Debtors—Open Accounts	2,500	0	0		
C	1,000	0	0	Bills Receivable	500	0	0		
				Cash at Bank	1,250	0	0		
				Cash in hand	50	0	0		
	£ 7,700	0	0		£ 7,700	0	0		

The partners share profits in the following proportions—A $\frac{1}{2}$, B $\frac{1}{3}$ rd, C $\frac{1}{6}$ th.

A retires, and B and C continue the business. It is agreed that the goodwill of the business shall be taken at a value of £3,000. The following Journal entry will then be made—

	£	s.	d.		£	s.	d.
Goodwill Account	Dr.	1,500	0	0			
to A.—Capital Account					1,500	0	0
for A's share of the Goodwill as agreed.							

A's Capital Account will then stand at £4,500. It will be observed that as B and C are continuing the business, it is not necessary, or advisable,

to credit their Capital Accounts with their respective shares of the goodwill.

If it is agreed that A's share shall be purchased by the continuing partners in certain proportions (e.g. the proportions in which they share profits), then in accordance with the decision in *Elliott v. Elliot* (see p. 758), the Capital Account of A should be transferred to the Capital Accounts of B and C in those proportions, and must not remain in the books of the firm as a debt due from the firm. This will necessitate making the following Journal entry—

	Dr.	£	s.	d.	£	s.	d.
A. Capital Account		4,500	0	0			
to B. Capital Account					3,000	0	0
to C. " "					1,500	0	0
for their respective shares of							
A's capital taken over by							
them.							

They will then become personally indebted to A for these respective amounts.

If, however, it is agreed that A's share in the business shall be treated as a loan to the business, and be paid off by instalments, the following Journal entry will be necessary—

	Dr.	£	s.	d.	£	s.	d.
A. Capital Account		4,500	0	0			
to A. Loan Account					4,500	0	0
being transfer of A's share							
in the business on his							
retirement.							

A common method of providing cash for paying out a part or the whole of the deceased partner's capital, or share of goodwill, or both, is by means of assurance on the lives of the partners, either jointly or severally, and this method has the advantage of relieving the business of undue financial strain, some such relief being especially desirable when the surviving partner or partners are not in a position to introduce any large amount of fresh capital.

The premiums on such policies should be charged to Profit and Loss Account. When one of the partners dies, and the insurance money is received, it will be credited to the Capital Accounts of the deceased and surviving partners in the proportion in which they shared profits or losses. It does not, however, affect the question of the deceased partner's share of goodwill. This will be ascertained and credited to his Capital Account in the usual way. The object is merely to provide ready cash. In some cases only a part of the annual premium is written off to Profit and Loss Account, the balance being debited to a Policy Account as in Example 1. The Policy Account shows the surrender value of the policy and the amount transferred from Premium Account is the yearly increase of such surrender value. In such

case when the policy falls in the amount received will be credited to the Policy Account and the balance only divided between the partners as they share profits.

When an account for goodwill has been created in the partnership books, it is advisable to write it off over a period of years, but it depends upon the agreement between the partners whether this is or is not done.

DISSOLUTION OF PARTNERSHIP.—Partnership may be dissolved in the following events. (See Sections 32, 33, 34 and 35 of the P.A. 1890.)

(1) When a partnership is entered into for a fixed term it is dissolved on the expiration of that term, but it may be continued after the term has expired without any express new agreement, in which case it becomes a partnership at will, and "the rights and duties of the partners remain the same as they were at the expiration of the term so far as is consistent with the incidents of a partnership at will." (Sec. 27, P.A., 1890.)

(2) By the termination of an adventure or undertaking when the partnership is entered into for a single adventure or undertaking.

(3) By notice where the partnership is entered into for an indefinite time. In this case a partner can terminate the partnership by giving notice to the other partner or partners, and the partnership is dissolved as from the date mentioned in the notice, or if no date be mentioned, as from the date of the communication of the notice.

(4) By the death of a partner subject to any agreement to the contrary.

(5) By bankruptcy of a partner subject to any agreement to the contrary.

(6) At the option of the other partners, if any partner suffers his share of the partnership property to be charged for his separate debt.

(7) By the happening of any event which makes it unlawful for the business of the firm to be carried on, or for the members of the firm to carry it on in partnership.

(8) By a decree of the Court on the application of a partner in any of the following cases—

(a) When a partner is found lunatic by inquisition.

(b) When a partner other than the partner making the application becomes in any other way permanently incapable of performing his part of the particular contract.

(c) When a partner other than the partner suing has been guilty of such conduct as in the opinion of the Court is calculated to affect prejudicially the carrying on of the business.

(d) When a partner, other than the partner suing, wilfully or persistently commits a breach of the partnership agreement.

(e) When the business of the partnership can only be carried on at a loss.

(f) Whenever in the opinion of the Court

circumstances have arisen which render it just and equitable that the partnership be dissolved.

As to the disposition of the partnership property in the event of a dissolution Section 44 of the Partnership Act, 1890, provides that in the absence of an agreement between the partners, to the contrary, the following rules shall be observed—

(1) Losses, including losses and deficiencies of capital, shall be paid, first out of profits, next out of capital, and lastly, if necessary, by the partners individually in the proportion in which they were entitled to share profits.

(2) The assets of the firm, including the sums—if any—contributed by the partners to make up losses or deficiencies of capital, shall be applied in the following manner—

(a) In paying the debts and liabilities of the firm to persons who are not partners therein.

(b) In paying to each partner rateably what is due from the firm to him for advances as distinguished from capital.

(c) In paying to each partner rateably what is due from the firm to him in respect of capital.

(d) The ultimate residue—if any—shall be divided amongst the partners in the proportion in which profits are divisible.

In dealing with the accounts of a firm in the event of a dissolution, the following is the best method to pursue—

(1) Make out a Balance Sheet as at the date of dissolution.

(2) Open a Realisation Account to which the assets, exclusive of cash, should be debited.

(3) Credit the Realisation Account with the amount realised by the sale of the assets, cash being thus debited, unless certain of the assets are taken over by one or other of the partners, in which case the amount at which they are taken over will be credited to the Realisation Account and debited to that partner's Capital Account.

(4) Pay off the sundry creditors out of cash, the total of discounts and allowances thereon being credited to the Realisation Account.

(5) Pay all the costs and expenses of realisation out of cash, the amount thereof being debited to the Realisation Account.

(6) The balance of this account will then show the net profit or loss on realisation, and this will be transferred to the credit or debit of the partners' Capital Accounts in the proportion in which they share profits or losses.

(7) If after this the Capital Account of any of the partners shows a debit balance, that partner must pay in cash to that amount, or if there be anything due to him for advances, a transfer should be made from the Advances Account to the Capital Account of the sum required.

(8) The partners' Advances Accounts must be paid off.

(9) The balance of cash will then equal the amount standing to the credit of the partners' Capital Accounts.

If a partner whose Capital Account is in debit, is unable to pay the amount shown to be due by him to the firm, then the rule in *Garner v. Murray* will apply, and the cash will be divided between the solvent partners in the proportions of their original or agreed capitals.

1. Example of a dissolution where the realisation of the assets results in a profit.

Brown and Smith are in partnership, sharing profits in the proportions of $\frac{2}{3}$ to Brown and $\frac{1}{3}$ to Smith, in accordance with the Partnership Deed. On 31st December, 19.., their Balance Sheet was as follows—

LIABILITIES.			ASSETS.		
	£	s. d.		£	s. d.
Sundry Creditors	850	0 0	Sundry Debtors	950	0 0
Bills Payable	350	0 0	Bills Receivable	300	0 0
Loan Account—			Cash at Bank	550	0 0
Brown	400	0 0	Cash in hand	50	0 0
Capital Accounts—			Stock-in-Trade	2,000	0 0
Brown	2,400	0 0	Fittings and Fix-		
Smith	1,200	0 0	tures	250	0 0
			Plant and Machin-		
			ery	1,100	0 0
	£ 5,200	0 0		£ 5,200	0 0

On 31st January, 19.., the assets of the business were sold to a firm of competitors at the following figures—

	£	s. d.		£	s. d.
Sundry Debtors	900	0 0	Bills Receivable	300	0 0
Stock-in-Trade	2,200	0 0	Fittings and Fixtures	350	0 0
Plant and Machinery	1,450	0 0			

The expenses of realising the above assets, and of writing up and closing the books of the firm, were £84.

The creditors were paid off on 31st January, 19.., and a sum of £36 was received by way of discount.

The Loan Account was paid off on 1st February, 19.., and the final settlement between the partners was effected on 28th February, 19..

The accounts of the partnership, when written up, will appear as follows—

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		£	s. d.	£	s. d.
19..					
Jan. 1	Realisation Account . . . Dr.	4,600	0 0		
	to Sundry Accounts				
	for Assets transferred.				
	Sundry Debtors			950	0 0
	Bills Receivable			300	0 0
	Stock-in-Trade			2,000	0 0
	Fittings and Fixtures			250	0 0
	Plant and Machinery			1,100	0 0
Jan. 31	Sundry Creditors " . . . Dr.	36	0 0		
	To Realisation Account			36	0 0
	for Discounts Received				

Dr.		REALISATION ACCOUNT										Cr.			
19..		£	s.	d.	£	s.	d.	19..		£	s.	d.	£	s.	d.
Jan. 1	To Assets transferred :							Jan. 31	By Proceeds from sale of :						
	Sundry Debtors .	950	0	0					Sundry Debtors .	900	0	0			
	Bills Receivable .	300	0	0					Bills Receivable .	300	0	0			
	Stock-in-Trade .	2,000	0	0					Stock-in-Trade .	2,200	0	0			
	Fittings and Fixtures .	250	0	0					Fittings and Fixtures .	350	0	0			
	Plant and Machinery .	1,100	0	0					Plant and Machinery .	1,450	0	0			
					4,600	0	0						5,200	0	0
Feb. 28	„ Realisation Expenses .				84	0	0		„ Discounts for Creditors .				36	0	0
	„ Balance—Profit, Brown, 2/3rds share .	368	0	0											
	Smith, 1/3rd share .	184	0	0											
					552	0	0								
					£ 5,236	0	0						£ 5,236	0	0

CASH AND BANK ACCOUNT

19..		£	s.	d.	19..		£	s.	d.
Jan. 1	To Balance in hand .	550	0	0	Jan. 31	By Sundry Creditors .	814	0	0
	„ Cash in hand .	50	0	0		„ Bills Payable .	350	0	0
„ 31	„ Sundry Debtors .	900	0	0	Feb. 1	„ Brown—Loan .	400	0	0
	„ Bills Receivable .	300	0	0	„ 28	„ Cost of Realisation .	84	0	0
	„ Stock-in-Trade .	2,200	0	0		„ Brown—Capital .	2,768	0	0
	„ Fittings and Fixtures .	350	0	0		„ Smith— „ .	1,384	0	0
	„ Plant and Machinery .	1,450	0	0					
		£ 5,800	0	0			£ 5,800	0	0

BROWN—CAPITAL ACCOUNT

19..		£	s.	d.	19..		£	s.	d.
Feb. 28	To Cash	2,768	0	0	Jan. 1	By Balance	2,400	0	0
					Feb. 28	„ Realisation A/c—Share of Profit .	368	0	0
		£ 2,768	0	0			£ 2,768	0	0

SMITH—CAPITAL ACCOUNT

19..		£	s.	d.	19..		£	s.	d.
Feb. 28	To Cash	1,384	0	0	Jan. 1	By Balance	1,200	0	0
					Feb. 28	„ Realisation A/c—Share of Profit .	184	0	0
		£ 1,384	0	0			£ 1,384	0	0

SUNDRY CREDITORS

19..		£	s.	d.	19..		£	s.	d.
Jan. 31	To Cash	814	0	0	Jan. 1	By Balance	850	0	0
	„ Discounts	36	0	0					
		£ 850	0	0			£ 850	0	0

2. Example of a dissolution where the realisation of the assets results in a loss.

Bush and Twigg are in partnership, sharing the profits in the ratio of $\frac{2}{3}$ ths to Bush, and $\frac{1}{3}$ ths to Twigg. They decide to discontinue business on 31st December, 19.., when their Balance Sheet was as follows—

LIABILITIES.			ASSETS.		
	£	s. d.		£	s. d.
Creditors . . .	800	0 0	Bank . . .	2,000	0 0
Bills Payable . .	1,000	0 0	Fittings . . .	300	0 0
Loan Account—			Stock . . .	2,400	0 0
Bush . . .	2,000	0 0	Debtors . . .	2,800	0 0
Capital Accounts—					
Bush . . .	2,000	0 0			
Twigg . . .	1,700	0 0			
	<u>£7,500</u>	<u>0 0</u>		<u>£7,500</u>	<u>0 0</u>

The fittings and stock are sold by auction, on 31st January, 19.., realising £2,100, the expenses of the sale being £112. During January the book debts are collected, with the exception

of £200 which proves to be bad, and a sum of £85 was allowed by way of discount. The creditors and bills payable are also paid off, £35 being received from the creditors for discount. The costs of the realisation amount to £53. Bush's Loan Account is paid off on 1st February, 19.., and the dissolution is completed on 20th February, 19..

The Journal Realisation Account, Bank Account, and the Partners' Accounts will appear as follows—

JOURNAL					
		£	s. d.	£	s. d.
19..					
Jan. 1	Realisation Account . . . Dr.	5,500	0 0		
	to Sundry Accounts				
	for Assets transferred				
	Fittings . . .			300	0 0
	Stock . . .			2,400	0 0
	Debtors . . .			2,800	0 0
Jan. 31	Sundry Creditors . . . Dr.	35	0 0		
	to Realisation Account				
	for discounts received			35	0 0

REALISATION ACCOUNT					
Dr.			Cr.		
	£	s. d.		£	s. d.
19..			19..		
Jan. 1	To Assets transferred		Jan. 31	By Proceeds of Sale of	
	Fittings . . .	300 0 0		Stock & Fittings	2,100 0 0
	Stock . . .	2,400 0 0		Cash from Debtors	2,515 0 0
	Debtors . . .	2,800 0 0		Discount from	
				Creditors . . .	35 0 0
		5,500 0 0	Feb. 28	Balance—Loss	
" 31	Expenses of Sale . .	112 0 0		3/5ths share to	
Feb. 28	Realisation Expenses . .	53 0 0		Bush . . .	609 0 0
				2/5ths share to	
		165 0 0		Twigg . . .	406 0 0
		£ 5,665 0 0			1,015 0 0
					£ 5,665 0 0

BANK ACCOUNT

	£	s. d.		£	s. d.
19..			19..		
Jan. 1	To Balance . . .	2,000 0 0	Jan. 31	By Expenses of Sale . .	112 0 0
" 31	Sale of Stock and			Bills Payable . . .	1,000 0 0
	Fittings . . .	2,100 0 0		Sundry Creditors . .	765 0 0
	Debtors . . .	2,515 0 0	Feb. 1	Bush—Loan A/c . .	2,000 0 0
			" 28	Realisation	
				Expenses . . .	53 0 0
				Bush—Capital A/c	1,391 0 0
				Twigg— " "	1,294 0 0
		£ 6,615 0 0			£ 6,615 0 0

BUSH—CAPITAL ACCOUNT

	£	s. d.		£	s. d.
19..			19..		
Feb. 28	To Realisation A/c—		Jan. 1	By Balance . . .	2,000 0 0
	Share of Loss . . .	609 0 0			
	Cash . . .	1,391 0 0			
		£ 2,000 0 0			£ 2,000 0 0

Dr.		TWIGG—CAPITAL ACCOUNT										Cr.			
19..					£	s.	d.	19..				£	s.	d.	
Feb. 28	To Realisation A/c—				406	0	0	Jan. 1	By Balance			1,700	0	0	
	Share of Loss				1,294	0	0								
	„ Cash														
					£	1,700	0	0				£	1,700	0	0

SUNDRY CREDITORS

19..					£	s.	d.	19..					£	s.	d.	
Jan. 31	To Cash	.	.	.	765	0	0	Jan. 1	By Balance	.	.	.	800	0	0	
	„ Discounts	.	.	.	35	0	0									
					£	800	0	0					£	800	0	0

In practice, as a rule, instead of transferring the balances standing to the debit of the various assets to the Realisation Account, the amounts received are posted to the credit of the respective assets and the balances only transferred to Realisation Account as shown in the following example—

3. Example of a dissolution where the realisation of the assets results in a loss, and one of the partners' Capital Accounts being in debit, he pays in cash to the amount thereof.

A, B and C are equal partners in a business. Their Balance Sheet on 31st December, 19.., was as follows—

LIABILITIES.				ASSETS.			
	£	s.	d.		£	s.	d.
Creditors . .	4 000	0	0	Land and Buildings	6 000	0	0
Bank Overdraft . .	1 000	0	0	Machinery and Plant	8 000	0	0
Loan Accounts—				Loose Tools . .	2 000	0	0
Creditors . .	14 000	0	0	Stock-in-Trade . .	7 000	0	0
A	2 500	0	0	Debtors . .	7 000	0	0
Capital Accounts—				Capital Account—			
A	6 000	0	0	C	1 000	0	0
B	3 500	0	0				
	£ 31 000	0	0		£ 31 000	0	0

On 31st January, 19.., the following assets were sold to a firm of rival manufacturers, at the figures shown—

Land and Buildings	£	6,500	0	0
Machinery and Plant	£	7,000	0	0
Loose Tools	£	1,500	0	0

The stock-in-trade was sold by auction on 16th February, 19.., the net amount received from the auctioneer being £6,800.

The book debts were collected during February, the net cash received being £6,800.

The creditors were paid off on 28th February, 19.., less £160 allowed as discount.

The creditors for loans were paid off in full on 28th February, 19.., plus £140 for interest in lieu of notice.

The expenses of dissolution of the business amounted to £120.

The dissolution was concluded on 10th March, 19.., when A's Loan Account was paid off, and C brought in the amount to which his Capital Account was in debit.

The closing entries will be as follows—

Dr.		LAND AND BUILDINGS										Cr.		
19..					£	s.	d.	19..				£	s.	d.
Jan. 1	To Balance . . .				6,000	0	0	Jan. 31	By Cash . . .			6,500	0	0
" 31	" Realisation A/c—													
	Profit on Sale . .				500	0	0							
					£6,500	0	0					£6,500	0	0

MACHINERY AND PLANT

19..					£	s.	d.	19..				£	s.	d.
Jan. 1	To Balance	.	.		8,000	0	0	Jan. 31	By Cash	.	.	7,000	0	0
									" Realisation A/c—					
									Loss on Sale	.	.	1,000	0	0
					£8,000	0	0					£8,000	0	0

Dr.				LOOSE TOOLS				Cr.				
19..				£	s.	d.	19..			£	s.	d.
Jan. 1	To Balance	.	.	2,000	0	0	Jan. 31	By Cash	.	1,500	0	0
								" Realisation A/c—		500	0	0
								Loss on Sale	.			
				£2,000	0	0				£2,000	0	0

STOCK-IN-TRADE

19..			£	s.	d.	19..		£	s.	d.
Jan. 1	To Balance . .		7,000	0	0	Feb. 16	By Cash . .	6,800	0	0
						" 28	" Realisation A/c—			
							Loss on Sale .	200	0	0
			£7,000	0	0			£7,000	0	0

SUNDRY DEBTORS

19..			£	s.	d.	19..		£	s.	d.
Jan. 1	To Balance . .		7,000	0	0	Feb. 28	By Cash . .	6,800	0	0
							" Realisation A/c—			
							Discounts and			
							Bad Debts .	200	0	0
			£7,000	0	0			£7,000	0	0

SUNDRY CREDITORS

19..			£	s.	d.	19..		£	s.	d.
Feb. 28	To Cash . .		3,840	0	0	Jan. 1	By Balance . .	4,000	0	0
	" Realisation A/c—									
	Discounts									
	received .		160	0	0					
			£4,000	0	0			£4,000	0	0

LOAN ACCOUNTS—CREDITORS

19..			£	s.	d.	19..		£	s.	d.
Feb. 28	To Cash . .		14,140	0	0	Jan. 1	By Balances . .	14,000	0	0
							" Realisation A/c—			
							Interest in lieu of			
							notice . .	140	0	0
			£14,140	0	0			£14,140	0	0

BANK ACCOUNT

19..			£	s.	d.	19..		£	s.	d.
Jan. 31	To Land & Buildings		6,500	0	0	Jan. 1	By Balance . .	1,000	0	0
	" Machinery & Plant		7,000	0	0	Feb. 28	" Sundry Creditors .	3,840	0	0
	" Loose Tools . .		1,500	0	0		" Loan Accounts—			
Feb. 16	" Stock-in-Trade .		6,800	0	0		" Creditors . .	14,140	0	0
" 28	" Sundry Debtors .		6,800	0	0	Mar. 10	" A—Loan Account	2,500	0	0
Mar. 10	" C—Repayment of						" Costs of dissolution	120	0	0
	amount over-						" A—Capital			
	drawn on Capital						Account . .	5,500	0	0
	Account . .		1,500	0	0		" B— do. . .	3,000	0	0
			£ 30,100	0	0			£ 30,100	0	0

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19..	Feb. 28	Realisation Account Dr.	£	1,900	s.	0	d.	0	£	s.	d.
		to Sundry Assets									
		for losses on sale of sundry assets—									
		Machinery and Plant							1,000	0	0
		Loose Tools							500	0	0
		Stock-in-Trade							200	0	0
		to Sundry Debtors							200	0	0
		for Discounts and Bad Debts									
Feb.	28	Land and Buildings Dr.		500	0	0			500	0	0
		to Realisation Account									
		for profit on sale									
Feb.	28	Sundry Creditors Dr.		160	0	0			160	0	0
		to Realisation Account									
		for discounts received									
Feb.	28	Realisation Account Dr.		140	0	0			140	0	0
		to Loan Accounts—Creditors									
		for interest in lieu of notice									

Dr.		REALISATION ACCOUNT										Cr.				
19..		£	s.	d.	£	s.	d.	19..		£	s.	d.	£	s.	d.	
Feb. 28	To Sundry Assets—							Feb. 28	By Land & Buildings—							
	Losses on								Profit on Sale .				500	0	0	
	Realisation—								Sundry Creditors .				160	0	0	
	Machinery and								Discounts .							
	Plant .	1,000	0	0					Balance—Loss .							
	Loose Tools .	500	0	0				Mar. 10	A—Capital A/c,							
	Stock-in-Trade .	200	0	0					B— do. 1 rd	500	0	0				
	Sundry Debtors .	200	0	0					C— do. 1 rd	500	0	0				
					1,900	0	0						1,500	0	0	
	„ Loan Accounts—															
	Creditors Interest				140	0	0									
	in lieu of notice .				120	0	0									
Mar. 10	„ Costs of Dissolution															
					£2,160	0	0						£	2,160	0	0

A—CAPITAL ACCOUNT

19..	Mar. 10	To Share of Loss	£	s.	d.	19..	Jan. 1	By Balance	£	s.	d.
		„ Cash	500	0	0				6,000	0	0
			5,500	0	0						

B—CAPITAL ACCOUNT

19..	Mar. 10	To Share of Loss	£	s.	d.	19..	Jan. 1	By Balance	£	s.	d.
		„ Cash	500	0	0				3,500	0	0
			3,000	0	0						

C—CAPITAL ACCOUNT

19..	Jan. 1.	To Balance	£	s.	d.	19..	Mar. 10	By Cash	£	s.	d.
Mar. 10		„ Share of Loss	1,000	0	0				1,500	0	0
			500	0	0						

Dr.		A—LOAN ACCOUNT						Cr.	
19..									
Mar. 10	To Cash			£	s.	d.	19..		
				2,500	0	0	Jan. 1	By Balance	

NOTES ON "GARNER v. MURRAY."—Until the decision of Mr. Justice Joyce in the case of *Garner v. Murray* [1904] 1 Ch. 57, 60, where, on a dissolution, the capital of one of the partners showed a deficiency, and such partner was insolvent and unable to contribute the amount due from him, such deficiency was treated as a loss of the business, and was borne by the solvent partners in the proportions in which they shared profits.

The position of affairs in the case in question, was as follows—

Garner, Murray, and Wilkins had entered into a partnership in 1900 on the terms that the capital of the business should be contributed in unequal shares, and that each partner should be entitled to $\frac{1}{3}$ rd share of the net profits.

By an order dated 14th May, 1901, the partnership was dissolved as from 30th June, 1900. The state of affairs after realising the assets and paying the liabilities of the partnership, was practically as follows—

BALANCE SHEET

LIABILITIES.			ASSETS.		
Capital—Garner .	£	s. d.	Cash	£	s. d.
" Murray .	2,500	0 0	Wilkins's Capital .	1,916	0 0
	314	0 0	A/c overdrawn .	263	0 0
			Loss on Realisation	635	0 0
	£2,814	0 0		£2,814	0 0

Nothing could be recovered from Wilkins.

Prior to the decision in this case, the method of dealing with this matter, would have been to treat the deficiency of Wilkins as a loss on realisation, making the total loss £898. This would have been charged— $\frac{1}{3}$ to Garner, and $\frac{1}{3}$ to Murray, i.e. £449 each, and debited to their respective capital accounts. Murray's Capital Account would therefore have shown a debit balance of £135, and Garner's Capital Account would have shown a credit balance of £2,051. Garner would have taken the whole of the cash £1,916, and Murray would have paid him the amount due in respect of his Capital Account £135, making up the £2,051 to which he was entitled.

Mr. Justice Joyce, however, decided that the deficiency of the third partner was not a deficiency of assets to be borne by the solvent partners in the same proportion as they bore profits and losses, but that "the assets must be applied in paying

to each partner rateably what was due from the firm to him in respect of capital, account being taken of the equal contributions to be made by him towards the deficiency of capital."

The word "losses" in Section 44 (a) of the P.A. 1890, means losses sustained by the firm, and Section 44 (b) proceeds on the supposition that contributions have been paid or levied.

The exact meaning of this decision, and the proper method of giving effect to it, have been the subject of much controversy amongst accountants.

The simplest and most reasonable method seems to be to treat the solvent partners as debtors of the firm for the amounts due from them as their share of the loss on realisation, and to divide the total amount of cash and indebtedness of the solvent partners, in the proportions of their respective capitals. The amount of cash taken by each partner will then be his proportion of the assets so ascertained, less the amount due from him as his share of the loss on realisation.

Applying this to the Balance Sheet of *Garner v. Murray* above, it would appear as follows—

LIABILITIES.			ASSETS.		
Garner—Capital A/c	£	s. d.	Cash	£	s. d.
Murray—	2,500	0 0	Garner's share of	1,916	0 0
"	314	0 0	loss— $\frac{1}{3}$ rd of £635	212	0 0
			Murray's do.	212	0 0
			Divisible Assets	2,340	0 0
			Wilkins's deficiency		
			of capital £263		
			Share of loss on		
			realisation 211	474	0 0
	2,814	0 0		2,814	0 0

The amount of the divisible assets is £2,340. This must be shared between Garner and Murray in the proportions of their capital. Therefore, Garner is entitled to $\frac{3}{8}$ ths of £2,340, which amounts to £2,079. From this must be deducted the amount due from him as shown on the Balance Sheet, viz., £212, leaving his share of the actual cash £1,867.

Murray's share will be $\frac{5}{8}$ ths of £2,340, which amounts to £261. From this must be deducted his share of loss—£212, leaving the actual cash received by him £49.

As to what is the capital of the partners, is a question which requires some consideration. It

Dr.		CASH BOOK						Cr.		
19..		£	s.	d.	19..			£	s.	d.
Dec. 31	To Cash in hand and at Bank	1,400	0	0	Dec. 31	By Loan on Mortgage		400	0	0
	„ Freehold Property . .	1,300	0	0		„ Sundry Creditors .		2,900	0	0
	„ Sundry Debtors . .	3,500	0	0		„ Costs		300	0	0
	„ Stock	1,200	0	0		„ Balance down . .		4,100	0	0
	„ Horses, Carts, etc.	300	0	0						
		£7,700	0	0				£7,700	0	0
19..		£	s.	d.	19..			£	s.	d.
	To Balance brought down	4,100	0	0		By Brown—Balance of Drawing Account		550	0	0
	„ Robinson—Divi- dend of 6/8 in the £ on balance of his Capital Account £650	216	13	4		„ Jones—Balance of Drawing Account		200	0	0
						„ Brown—Capital Account $\frac{1}{2}$ of Bal- ance of Cash . .	2,229	3	4	
						„ Jones—Capital Account $\frac{1}{2}$ of Balance of Cash .	1,337	10	0	
		£4,316	13	4				3,566	13	4
								£4,316	13	4

SUNDRY DEBTORS' ACCOUNT

		£	s.	d.				£	s.	d.
19..					19..					
Dec. 31	To Sundry Debtors as per Ledgers . .				Dec. 31	By Realisation A/c .		4,000	0	0
	(Balance brought down) . .	4,000	0	0				<u>4,000</u>	0	0

SUNDRY CREDITORS' ACCOUNT

		£	s.	d.				£	s.	d.
19..					19..					
Dec. 31	To Cash . .	2,900	0	0	Dec. 31	By Sundry Creditors as per Ledgers . .				
	„ Discounts . .	100	0	0		(Balance brought down) . .		3,000	0	0
								<u>3,000</u>	0	0
		<u>3,000</u>	0	0						

STOCK-IN-TRADE

		£	s.	d.				£	s.	d.
19..					19..					
Dec. 31	To Stock at date . .	1,500	0	0	Dec. 31	By Realisation A/c .		1,500	0	0

HORSES, CARTS, ETC.

		£	s.	d.				£	s.	d.
19..					19..					
Dec. 31	To Sundries . .	500	0	0	Dec. 31	By Realisation A/c .		500	0	0

FREEHOLD PROPERTY

		£	s.	d.				£	s.	d.
19..					19..					
Dec. 31	To Freehold Property . .	1,000	0	0	Dec. 31	By Realisation A/c .		1,000	0	0

Dr.			LOAN ON MORTGAGE						Cr.		
19..			£	s.	d.	19..			£	s.	d.
Dec. 31	To Cash		400	0	0	Dec. 31	By Loan on Mortgage of Freehold Property		400	0	0

BROWN—CAPITAL ACCOUNT

19..			£	s.	d.	19..			£	s.	d.
Dec. 31	To Cash, $\frac{3}{4}$ ths of balance of cash . .		2,229	3	4	Dec. 31	By Balance . . .		2,500	0	0
	„ Balance to Robinson—Capital A/c		270	16	8						
			<u>£2,500</u>	<u>0</u>	<u>0</u>				<u>£2,500</u>	<u>0</u>	<u>0</u>

BROWN—DRAWING ACCOUNT

19..			£	s.	d.	19..			£	s.	d.
Dec. 31	To Realisation A/c—Share of Loss . .		450	0	0	Dec. 31	By Balance . . .		1,000	0	0
	„ Cash		550	0	0						
			<u>£1,000</u>	<u>0</u>	<u>0</u>				<u>£1,000</u>	<u>0</u>	<u>0</u>

JONES—CAPITAL ACCOUNT

19..			£	s.	d.	19..			£	s.	d.
Dec. 31	To Cash, $\frac{3}{4}$ ths of Balance of cash . .		1,337	10	0	Dec. 31	By Balance . . .		1,500	0	0
	„ Robinson—Balance To Robinson—Capital A/c		162	10	0						
			<u>1,500</u>	<u>0</u>	<u>0</u>				<u>1,500</u>	<u>0</u>	<u>0</u>

JONES—DRAWING ACCOUNT

19..			£	s.	d.	19..			£	s.	d.
Dec. 31	To Realisation A/c—Share of loss . .		300	0	0	Dec. 31	By Balance . . .		500	0	0
	„ Cash		200	0	0						
			<u>£500</u>	<u>0</u>	<u>0</u>				<u>£500</u>	<u>0</u>	<u>0</u>

ROBINSON—CAPITAL ACCOUNT

19..			£	s.	d.	19..			£	s.	d.
Dec. 31	To Balance		500	0	0	Dec. 31	By Cash—Dividend of 6s. 8d. in the £ on £650 . .		216	13	4
	„ Realisation A/c—Share of loss . .		150	0	0		„ Brown, Capital A/c— $\frac{1}{4}$ of deficiency . .		270	16	8
							„ Jones, Capital A/c— $\frac{1}{4}$ of deficiency . .		162	10	0
			<u>£650</u>	<u>0</u>	<u>0</u>				<u>£650</u>	<u>0</u>	<u>0</u>

NOTES ON "ELLIOTT v. ELLIOTT."—The case of *Elliott v. Elliott* (45 *Accountant Law Reports*, 47) is one of great interest and importance. In this case, which was decided by Mr. Justice Warrington in November, 1911, there were four partners, Stephen Elliott and his three sons, Alfred, Charles and George.

The Articles of Partnership, which were entered into in 1904, provided that upon the death of a partner, the other partners should take over his share and undertake the liabilities of the business, and for the purpose of ascertaining that share, the goodwill was to be taken into account at £10,000. Alfred died in 1906, and this figure was taken as the value of goodwill in ascertaining his share.

It was pointed out that this amount of £10,000 was an absurd value to put upon the goodwill, and by a signed agreement between the surviving partners, the value of goodwill was fixed at £800.

The father, Stephen Elliott, died on the 10th September, 1910, and his executors claimed that the original figure of £10,000 must be taken in ascertaining his share as being the value of the goodwill. It was decided that the goodwill must be taken at the figure subsequently agreed upon by the partners, viz., £800.

In taking stock at the death of Alfred, the stock was taken as a whole, at selling price, and 30 per cent. deducted for the purpose of ascertaining the net value, and this practice was followed for the purpose of the Balance Sheets until the death of the father. On his death, a professional valuer was employed who valued the stock on a different footing, with the result that it came out at a considerably less sum than it would have done if the previous method had been adhered to.

It was argued for the executors of the father, that this valuation was not a proper one for the purpose, but that the parties were bound by their conduct to adopt the previous method of valuation.

It was held that the valuation at the death of the father was for a totally different purpose from the previous ones, and that the partners were, therefore, not bound to adopt the previous method of valuation and that it was right and proper that the stock should be taken at the value placed upon it by the valuer, which, it was admitted, was fair and just.

It was held that the Balance Sheets which had been audited by Chartered Accountants who were independent persons representing all the parties, and appointed on the nomination of the bank, were binding upon the father as much as upon the other partners, although he was an illiterate man who could not read or understand figures.

With regard to the amount due to the executors of Alfred, it had been contended that this was a

partnership liability. It had been treated as such in the books of the partnership, and payment had been made out of the partnership assets to Alfred's executors. It was held that the parties were not entitled to go back and treat the payment to Alfred's executors as having been wrongly paid out of the partnership assets, but that as regarded the balance then owing, it was not a partnership debt, but a personal liability of the individual partners, and must therefore be struck out of the Balance Sheet.

The father had withdrawn large sums from the business in excess of his share of profits. The partnership Articles provided that every year, the excess of drawings over the share of profits, should be refunded. This had not been done, but the amounts overdrawn had been debited against his capital, and it was contended that by so doing, the partners had discharged him from the liability to refund. The judge held that this was not so, and that the overdrawings must be refunded, and that therefore, in now ascertaining the value of the assets for the purpose of finding what was due to the father, the amount which he had overdrawn must be taken into account, as an asset of the firm.

The chief point which calls for notice in this decision, is that which relates to the treatment of the amount due to the executors of a deceased partner. The effect on the accounts of a partnership will be that when the amount of the deceased partner's share has been ascertained in accordance with the terms of the agreement, the amount standing to his credit will have to be transferred to the credit of the other partners' Capital Accounts in the proportions in which they share profits, and the account of the deceased partner thereby eliminated from the books of the partnership.

Surviving partners will accordingly have their respective capitals increased but will be personally liable to the estate of the deceased partner for his share in the capital of the business.

The latter part of this decision, referring to the refunding of overdrawn amounts, should also be carefully noted.

V. Dissolution of Partnership—Payments to Partners on account of Capital. It sometimes happens that the realisation of the partnership estate occupies a considerable period, and partial realisations from time to time result in the accumulation of considerable sums of cash. Under these circumstances, it is usual to make interim distributions, and the best method to pursue in such cases, is to proceed by appropriating the earlier distributions in reducing the capitals of the partners until they bear the same relation to one another as the proportions in which they share profits. When they have been so reduced, the further distributions will take place in the proportions in which profits are shared, and the final

balances on the Capital Accounts, after realisation of the assets and the distribution of the proceeds, will, together, be equal to the profit or loss on realisation shown by the Realisation Account, which profit or loss cannot be ascertained until the realisation has been completed.

Where there is a great disparity between the amount of one partner's capital and that of the others, it will be necessary to proceed cautiously, taking care to retain in hand a sufficient sum to adjust the accounts in accordance with the decision in *Garner v. Murray*, in case the loss on realisation should place the capital of one of the partners in debit, and he should be unable to repay the amount so shown to be owing by him to the firm.

The following is an example showing the working of this method—

BALANCE SHEET, 31ST DECEMBER, 19..									
LIABILITIES.					ASSETS.				
	£	s.	d.		£	s.	d.		
Sundry Creditors .	4,000	0	0		Land and Buildings	3,000	0	0	
Capital—A	£8,000				Machinery, Plant				
B	6,000				and Loose Tools	1,050	0	0	
C	5,000				Stock-in-Trade	2,600	0	0	
	19,000	0	0		Sundry Debtors	5,800	0	0	
					Investments	10,000	0	0	
					Cash in hand and				
					at Bank	550	0	0	
	£ 23,000	0	0			£ 23,000	0	0	

Profits and losses were divided—A $\frac{1}{2}$, B $\frac{5}{8}$ ths, C $\frac{1}{8}$ ths.

The assets (excluding cash in hand and at bank) realised £18,950, and the expenses of realisation amounted to £500. By 1st March, 19.., £9,000 had been received on account, and the creditors were then paid off, and £4,000 was paid to the partners on account. By May 1st, a further amount of £5,000 had been received on account, and a further distribution of £4,000 on account was made. The balance of the realisation moneys was all received by 30th June, 19.., on which date the final distribution took place.

In this example, it will be noticed that the partners share profits in the proportions of $\frac{8}{16}$ ths, $\frac{5}{16}$ ths, and $\frac{1}{16}$ ths, so that following the method suggested, it would be necessary to reduce their capitals in the first instance, to £8,000, £5,000 and £3,000. This will be effected as shown, by paying to B £1,000 and to C £2,000 out of the first distribution. The balance of the distribution will be divided in the proportions in which the partners share profits, and future distributions will also be divided in those proportions.

CHANGE IN PARTNERSHIP.—When a partner retires from a firm, he must, in order to relieve himself from further liability, give notice of his retirement to all persons who have had dealings with the firm, and in addition, a notice of the

Dr.												LAND AND BUILDINGS												Cr.																																																																																																																																															
19..												£												s.												d.												19..												£												s.												d.																																																																																			
Dec. 31												To Balance												.												.												3,000												0												0												Dec. 31												By												Transfer to												Realisation A/c												3,000												0												0											

MACHINERY, PLANT AND LOOSE TOOLS													
19..				£	s.	d.	19..				£	s.	d.
Dec. 31	To Balance	.	.	1,050	0	0	Dec. 31	By Transfer to			1,050	0	0
								Realisation A/c					

STOCK-IN-TRADE											
19..				£		s.		d.		19..	
Dec. 31	To Balance	.	.	2,600	0	0	Dec. 31	By Transfer to		£	s.
								Realisation A/c		2,600	0
										0	0

SUNDRY DEBTORS												
19..				£	s.	d.	19..			£	s.	d.
Dec. 31	To Balances	.	.	5,800	0	0	Dec. 31	By Transfer to Realisation A/c		5,800	0	0

Dr.		INVESTMENTS						Cr.	
19..		£	s.	d.	19..		£	s.	d.
Dec. 31	To Balance . . .	10,000	0	0	Dec. 31	By Transfer to Realisation A/c .	10,000	0	0

SUNDRY DEBTORS

19..		£	s.	d.	19..		£	s.	d.
Mar. 1	To Cash . . .	4,000	0	0	Dec. 31	By Balance . . .	4,000	0	0

REALISATION ACCOUNT

19..		£	s.	d.	19..		£	s.	d.
Dec. 31	To Land & Buildings .	3,000	0	0	Mar. 1	By Cash . . .	9,000	0	0
	" Machinery, Plant and Loose Tools .	1,050	0	0	May 1	" . . .	5,000	0	0
	" Stock-in-Trade .	2,600	0	0	June 30	" . . .	4,950	0	0
	" Sundry Debtors .	5,800	0	0		" Balance being Loss	4,000	0	0
	" Investments .	10,000	0	0					
June 30	" Realisation Expenses .	500	0	0					
		£ 22,950	0	0			£ 22,950	0	0
19..		£	s.	d.	June 30	By Capital Accounts—	£	s.	d.
June 30	To Balance . . .	4,000	0	0		A. $\frac{1}{2}$. . .	2,000	0	0
						B. $\frac{5}{16}$. . .	1,250	0	0
						C. $\frac{3}{16}$. . .	750	0	0
		£ 4,000	0	0			4,000	0	0
		£ 4,000	0	0			£ 4,000	0	0

CASH ACCOUNT.

19..		£	s.	d.	19..		£	s.	d.
Dec. 31	To Balance . . .	550	0	0	Mar. 1	By Creditors . . .	4,000	0	0
19..						Capital Accounts—			
Mar. 1	" Realisation A/c .	9,000	0	0		A— $\frac{1}{2}$ of £1,000 .	500	0	0
May 1	" . . .	5,000	0	0		B— $\frac{1}{16}$ of £1,000 +			
June 30	" . . .	4,950	0	0		5/16 of £1,000 .	1,312	10	0
						C—£2,000 +			
						3/16 of £1,000 .	2,187	10	0
					May 1	" Capital Accounts—			
						A— $\frac{1}{2}$ of £4,000 .	2,000	0	0
						B— $\frac{5}{16}$ of £4,000 .	1,250	0	0
						C— $\frac{3}{16}$ of £4,000 .	750	0	0
					June 30	" Realisation Expenses . . .	500	0	0
					June 30	" Capital Accounts—			
						A— $\frac{1}{2}$ of balance	3,500	0	0
						B— $\frac{5}{16}$. . .	2,187	10	0
						C— $\frac{3}{16}$. . .	1,312	10	0
		£ 19,500	0	0			£ 19,500	0	0

CAPITAL ACCOUNTS

Dr.				A		Cr.			
19..				£	s. d.	19..		£	s. d.
Mar. 1	To Cash			500	0 0	Dec. 31	By Balance	8,000	0 0
May 1	" "			2,000	0 0				
June 30	" Loss on Realisation			2,000	0 0				
	" Cash			3,500	0 0				
				<u>£8,000</u>	<u>0 0</u>			<u>£8,000</u>	<u>0 0</u>

B

19..				£	s. d.	19..		£	s. d.
Mar. 1	To Cash			1,312	10 0	Dec. 31	By Balance	6,000	0 0
May 1	" "			1,250	0 0				
June 30	" Loss on Realisation			1,250	0 0				
	" Cash			2,187	10 0				
				<u>£6,000</u>	<u>0 0</u>			<u>£6,000</u>	<u>0 0</u>

C

19..				£	s. d.	19..		£	s. d.
Mar. 1	To Cash			2,187	10 0	Dec. 31	By Balance	5,000	0 0
May 1	" "			750	0 0				
June 30	" Loss on Realisation			750	0 0				
	" Cash			1,312	10 0				
				<u>£5,000</u>	<u>0 0</u>			<u>£5,000</u>	<u>0 0</u>

retirement must be advertised in the *London Gazette*.

A retiring partner is liable for all debts and liabilities of the firm incurred prior to his retirement, and for debts and liabilities incurred subsequent to that date, until he has given proper notice of his retirement, as any person who has had dealings with the firm, is entitled to treat all the old members of the firm as still being members, until he receives notice to the contrary.

If the outgoing partner's place is taken by an incoming partner, the incoming partner is not liable for the debts and liabilities of the firm incurred prior to the date on which he becomes a partner, but an incoming partner may agree to accept the existing liabilities, and if the creditors agree to accept the new firm thus constituted, in place of the old firm, the retiring partner will be relieved. There will then be a contract of substituted liability, which is termed "novation," but it must be clearly understood that such an agreement is a tripartite one, the parties thereto being—

1. A retiring partner.
2. The new firm.
3. The creditors.

To render this arrangement valid, the consent of the creditors is absolutely necessary. This consent need not be expressly given, but may be inferred from the course of dealing.

The new firm may agree to indemnify the retiring partner against any claim, and then if any of the creditors refuse to assent, and are paid by the retiring partner, the firm will have to repay him.

Where a partner retires, and the business is carried on by the remaining partners, and no new partner is introduced, there can be no novation, but under certain circumstances, the retiring partner may be discharged by accord and satisfaction, as in the case of *Thompson v. Percival* (5 B. & Ad. 925), where the business was carried on by two partners, and the partnership was dissolved, and it was agreed that one of the partners should continue to carry on the business, and receive and pay all debts. The plaintiff in this case was told that he must look to the continuing partner for payment, and accordingly drew a bill upon him, which was accepted, but was afterwards dishonoured. On suing both partners for the original debt, it was held that the retiring partner had been discharged by accord and satisfaction.

The following are two examples of change in partnership—

(1) Where one partner retires, and the remaining partners take over the assets at a valuation and continue the business.

(2) Where one partner retires, and another partner is admitted.

EXAMPLE 1

Where one partner retires, and the remaining partners take over the assets at a valuation and continue the business.

A, B, and C carry on business in partnership as timber merchants. On 31st December, 19.., the partnership was terminated by effluxion of time. The Balance Sheet of the firm at that date was as follows—

LIABILITIES.			ASSETS.		
	£	s. d.		£	s. d.
Sundry Creditors . .	700	0 0	Freehold Land and		
Bills Payable . .	1,800	0 0	Buildings (subject	8,000	0 0
Mortgage at 4% . .	6,000	0 0	to Mortgage contra)	2,000	0 0
Capital—			Plant and Machinery		
A £10,000			Loose Plant and		
B 5,000			Tools	400	0 0
C 2,500			Stock-in-Trade . .	10,000	0 0
	17,500	0 0	Horses, Carts and		
			Harness	600	0 0
			Sundry Debtors . .	3,500	0 0
			Cash in hand and		
			at Bank	1,500	0 0
	£26,000	0 0		£26,000	0 0

It was arranged that A and B should take over the business and pay C out on the following terms—

(1) The liabilities were to be taken over at the figures shown above.

(2) The assets were to be subject to the following adjustments—

(a) Land and buildings were valued at £8,500.

(b) Plant and machinery subject to 10 per cent. depreciation.

(c) Loose plant and tools, and horses, carts and harness, subject to 20 per cent. depreciation.

(d) Stock-in-Trade was agreed at £9,250.

(e) Sundry debtors subject to an allowance of £250.

The partners divided profits and losses in the proportions of A $\frac{1}{2}$, B $\frac{1}{3}$ rd, and C $\frac{1}{6}$ th.

The costs of realisation were to be paid by A and B.

The closing entries of the firm, A, B and C, will be as follows—

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19..		£	s. d.	£	s. d.
Jan. 1	Realisation Account Dr. to Sundry Assets for amounts transferred.	24,500	0 0		
	Freehold Land and Buildings			8,000	0 0
	Plant and Machinery			2,000	0 0
	Loose Plant and Tools			400	0 0
	Stock-in-Trade			10,000	0 0
	Horses, Carts and Harness			600	0 0
	Sundry Debtors			3,500	0 0
19..	A & B—Purchase Account Dr. to Realisation Account for Assets taken over at the following values—	23,600	0 0		
Jan. 1	Freehold Land and Buildings.			8,500	0 0
	Plant and Machinery £2,000 Less. Depreciation 10% 200			1,800	0 0
	Loose Plant & Tools £400 Less. Depreciation 20% 80			320	0 0
	Horses, Carts and Harness £600 Less. Depreciation 20% 120			480	0 0
	Stock-in-Trade			9,250	0 0
	Sundry Debtors £3,500 Less. Allowance 250			3,250	0 0
	Sundry Accounts Dr. to A & B—Purchase A/c for Liabilities taken over by them.			8,500	0 0
	Sundry Creditors	700	0 0		
	Bills Payable	1,800	0 0		
	Mortgage at 4%	6,000	0 0		

Dr.				REALISATION ACCOUNT.				Cr.			
19..		£	s. d.	£	s. d.	19..		£	s. d.	£	s. d.
Jan. 1	To Sundry Assets—					Jan. 1	By A & B Purchase				
	Freehold Land	8,000	0 0				Account for assets				
	and Buildings .						taken over				
	Plant and						Freehold Land .	8,500	0 0		
	Machinery .	2,000	0 0				and Buildings .				
	Loose Plant and						Plant and				
	Tools .	400	0 0				Machinery .	1,800	0 0		
	Stock-in-Trade .	10,000	0 0				Loose Plant and				
	Horses, Carts and						Tools .	320	0 0		
	Harness .	600	0 0				Horses, Carts and				
	Sundry Debtors .	3,500	0 0				Harness .	480	0 0		
				24,500	0 0		Stock-in-Trade .	9,250	0 0		
							Sundry Debtors .	3,250	0 0		
										23,600	0 0
						"	By Loss on Realisa-				
							tion—				
							A—Capital A/c, $\frac{1}{2}$	450	0 0		
							B— " $\frac{1}{3}$	300	0 0		
							C— " $\frac{1}{6}$	150	0 0		
										900	0 0
				£ 24,500	0 0					£ 24,500	0 0

Dr.		A & B—PURCHASE ACCOUNT						Cr.	
19..		£	s.	d.	19..		£	s.	d.
Jan. 1	To Sundry Assets taken over	23,600	0	0	Jan. 1	By Sundry Liabilities taken over	8,500	0	0
						„ A—Capital A/c	9,550	0	0
						„ B—	4,700	0	0
						„ Cash	850	0	0
		£ 23,600	0	0			£ 23,600	0	0

CASH BOOK

19..		£	s.	d.	19..		£	s.	d.
Jan. 1	To Balance in hand and at Bank	1,500	0	0	Jan. 1	By C—Capital A/c	2,350	0	0
	„ A & B	850	0	0					
		£ 2,350	0	0			£ 2,350	0	0

A—CAPITAL ACCOUNT

19..		£	s.	d.	19..		£	s.	d.
Jan. 1	To Realisation A/c—Share of Loss	450	0	0	Jan. 1	By Balance	10,000	0	0
	„ Balance to A & B—Purchase A/c	9,550	0	0					
		£ 10,000	0	0			£ 10,000	0	0

B—CAPITAL ACCOUNT

19..		£	s.	d.	19..		£	s.	d.
Jan. 1	To Realisation A/c—Share of Loss	300	0	0	Jan. 1	By Balance	5,000	0	0
	„ Balance to A & B—Purchase A/c	4,700	0	0					
		£ 5,000	0	0			£ 5,000	0	0

C—CAPITAL ACCOUNT

19..		£	s.	d.	19..		£	s.	d.
Jan. 1	To Realisation A/c—Share of Loss	150	0	0	Jan. 1	By Balance	2,500	0	0
	„ Cash	2,350	0	0					
		£ 2,500	0	0			£ 2,500	0	0

EXAMPLE 2

Where one partner retires, and another partner is admitted.

A, B and C carried on business in partnership for many years. A wished to retire, and it was arranged that he should do so as on 31st December, 19.., and that B and C should take over the business and admit D into partnership on the following terms—

A's capital in the old business to be treated as a loan to the new business.

D to pay to B and C £1,000 as premium, the amount to be divided between them in proportion as they shared profits, and the cash to be left in the business as additional working capital.

D to pay £2,000 for Capital.

In the old firm profits were shared—

A $\frac{1}{3}$ B $\frac{2}{3}$ C $\frac{2}{3}$

In the new firm profits were shared—

B $\frac{3}{4}$ C $\frac{1}{4}$ D $\frac{1}{4}$

The following is the Balance Sheet of A, B and C at 31st December, 19.., after adjustments of assets and liabilities taken over.

LIABILITIES.		ASSETS.	
B & C for amounts owing to Sundry Creditors. 10,000		B & C for the following	
Capital Account—		Assets taken over—	
A £10,000		Cash . . . £1,000	
B 6,000		Debtors . . . 12,000	
C 4,000		Stock . . . 9,500	
		Loose Tools . . 500	
		Machinery and Plant . . 7,000	
	20,000		30,000
			£ 30,000
	£30,000		£ 30,000

Presuming that D pays in the amount due from him for premium and capital on 1st January, 19.., the books of the new firm will be opened as follows—

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19..			£	s.	d.	£	s.	d.
Jan. 1								
	Sundry Assets	Dr.						
	to Sundry Liabilities and Capital—							
	Cash		1,000	0	0			
	Debtors		12,000	0	0			
	Stock-in-Trade		9,500	0	0			
	Loose Tools		500	0	0			
	Machinery and Plant		7,000	0	0			
	to Sundry Creditors—					10,000	0	0
	A—Loan Account					10,000	0	0
	B—Capital Account					6,000	0	0
	C—do.					4,000	0	0
			£ 30,000	0	0	£ 30,000	0	0
19..			£	s.	d.	£	s.	d.
Jan. 1			1,000	0	0			
	Premium Account	Dr.						
	to B—Capital Account					600	0	0
	C—do.					400	0	0
	being apportionment of premium paid by C							

Dr.		SUNDRY DEBTORS		Cr.
19..				
Jan. 1	To Balance taken over	£ 12,000	s. 0	d. 0

		STOCK-IN-TRADE		
19..				
Jan. 1	To Balance taken over	£ 9,500	s. 0	d. 0

		LOOSE TOOLS		
19..				
Jan. 1	To Balance taken over	£ 500	s. 0	d. 0

		MACHINERY AND PLANT		
19..				
Jan. 1	To Balance taken over	£ 7,000	s. 0	d. 0

		SUNDRY CREDITORS		
19..				
Jan. 1	By Balance taken over		£ 10,000	s. 0

		A—LOAN ACCOUNT		
19..				
Jan. 1	By Balance, being amount of Capital in old firm		£ 10,000	s. 0

Dr.		PREMIUM ACCOUNT				Cr.			
19..		£	s.	d.	19..	£	s.	d.	
Jan. 1	To B—Capital A/c	600	0	0	Jan. 1	By Cash	1,000	0	0
	„ C— do 2/5 „	400	0	0					
		<u>£1,000</u>	<u>0</u>	<u>0</u>			<u>£1,000</u>	<u>0</u>	<u>0</u>

CASH ACCOUNT									
19..		£	s.	d.	19..	£	s.	d.	
Jan. 1	To Balance taken over	1,000	0	0	Jan. 1	By Balance down .	4,000	0	0
	„ Premium Account	1,000	0	0					
	„ D—Capital „	2,000	0	0					
		<u>£4,000</u>	<u>0</u>	<u>0</u>			<u>£4,000</u>	<u>0</u>	<u>0</u>
19..									
Jan. 1	To Balance brought down . .	4,000	0	0					

B—CAPITAL ACCOUNT									
19..		£	s.	d.	19..	£	s.	d.	
Jan. 1	To Balance down . .	6,600	0	0	Jan. 1	By Balance from old firm	6,000	0	0
						„ Premium Account	600	0	0
		<u>£6,600</u>	<u>0</u>	<u>0</u>			<u>£6,600</u>	<u>0</u>	<u>0</u>
					19..				
					Jan. 1	By Balance brought down	6,600	0	0

C—CAPITAL ACCOUNT									
19..		£	s.	d.	19..	£	s.	d.	
Jan. 1	To Balance	4,400	0	0	Jan. 1	By Balance from old firm	4,000	0	0
						„ Premium Account	400	0	0
		<u>£4,400</u>	<u>0</u>	<u>0</u>			<u>£4,400</u>	<u>0</u>	<u>0</u>
					19..				
					Jan. 1	By Balance brought down	4,400	0	0

D—CAPITAL ACCOUNT									
					19..	£	s.	d.	
					Jan. 1	By Cash	2,000	0	0

B, C & D
BALANCE SHEET, 1st JANUARY, 19..

Liabilities.		£	s.	d.	£	s.	d.	Assets.		£	s.	d.
Sundry Creditors . .					10,000	0	0	Cash in hand		4,000	0	0
A—Loan Account . .					10,000	0	0	Debtors		12,000	0	0
Capital Accounts—								Stock-in-Trade . . .		9,500	0	0
B	6,600	0	0					Loose Tools		500	0	0
C	4,400	0	0					Machinery and Plant .		7,000	0	0
D	2,000	0	0									
					<u>13,000</u>	<u>0</u>	<u>0</u>					
					<u>£33,000</u>	<u>0</u>	<u>0</u>			<u>£33,000</u>	<u>0</u>	<u>0</u>

PAYMENTS

		£	s.	d.
19..				
Jan. 1	To Timber	1,000	0	0
"	" Freight and Charges . .	65	0	0
"	" Discount on Bill . . .	8	0	0
		<u>£1,073</u>	<u>0</u>	<u>0</u>

RECEIPTS

		£	s.	d.
19..				
Jan. 1	By Bills Receivable . . .	800	0	0
	" Balance—Excess of Payments over Receipts .	<u>£273</u>	<u>0</u>	<u>0</u>

Brown's Statement.—Statement of receipts and payments of Brown in connection with a Joint Adventure in timber with Smith.

RECEIPTS

		£	s.	d.
19..				
Feb. 1	By Timber sold—one-half .	670	0	0
" 17	" " " "	580	0	0
		<u>£1,250</u>	<u>0</u>	<u>0</u>

PAYMENTS

		£	s.	d.
19..				
Jan. 20	To Dock Dues, Landing Charges, etc.	£21		
Mar. 5	" Bills Payable—Cash . .	800		
		821	0	0
	" Balance—Excess of Receipts over Payments	429	0	0
		<u>£1,250</u>	<u>0</u>	<u>0</u>

From these statements, Brown draws up a Profit and Loss Account of the joint adventure, together with the accounts of himself and Smith, as follows, and on the 31st March, remits to Smith a banker's draft for the amount due to him—

JOINT ADVENTURE

PROFIT AND LOSS ACCOUNT

Dr.		PROFIT AND LOSS ACCOUNT								Cr.		
		£	s.	d.	£	s.	d.			£	s.	d.
Jan. 1	To Smith—							Feb. 1	By Brown—			
	Timber bought	1,000	0	0					Timber sold	670	0	0
	" " Freight paid	65	0	0				" 17	" " "	580	0	0
	" Smith—Discount on Bill				1,065	0	0					
	" Brown—Dock Dues				8	0	0					
					21	0	0					
					1,094	0	0			1,250	0	0
Mar. 31	" Profit—Balance— ½ share to Brown	78	0	0								
	" " Smith	78	0	0								
					156	0	0					
					£1,250	0	0			£1,250	0	0

JOURNAL ENTRIES

		£	s.	d.	£	s.	d.
19..							
Jan. 1	Joint Adventure Account Dr. to Smith	1,065	0	0			
	for Timber purchased by him and Freight thereon. Timber £1,000 Freight 65				1,065	0	0
19..							
Jan. 1	Smith Dr. to Brown	800	0	0			
	for bill at 60 days sight. . .				800	0	0
" "	Joint Adventure Account Dr. to Smith	8	0	0			
	for discount on bill.				8	0	0
" "	Joint Adventure Account Dr. to Brown	21	0	0			
	for Dock Dues, etc., paid. . .				21	0	0
Feb. 1	Brown Dr. to Joint Adventure Account for Timber sold.	670	0	0			
					670	0	0
" 17	Brown Dr. to Joint Adventure Account for Timber sold	580	0	0			
					580	0	0

LIMITED PARTNERSHIPS.—Prior to the Limited Partnership Act, 1907, no distinction existed as regards liability of various partners, even though one or more of them might be sleeping or dormant partners, but under the above mentioned Act, a firm can now consist of one or more general partners, and one or more limited partners.

General partners are liable for all debts and obligations of the firm in the same way as every partner was prior to this Act.

A limited partner, when he enters the partnership, agrees to contribute a certain amount in cash or property, and is not liable for any debts or obligations of the firm beyond the amount which he has agreed to contribute.

A limited partner must not draw out or receive back in any way, any part of his capital during the continuance of the partnership, and if he does so, he will be liable for the debts and obligations of the firm to the amount so received back, and moreover, a limited partner cannot dissolve the

Dr.			SMITH						Cr.					
19..			£	s.	d.	£	s.	d.	19..			£	s.	d.
Jan. 1	To Brown—Bill at 60 days' sight .					800	0	0	Jan. 1	By Joint Adventure Account—				
Mar. 31	„ Balance down .					351	0	0		Timber . .	1,000	0	0	
										Freight . .	65	0	0	
										„ Joint Adventure Account—				1,065 0 0
										Discount on Bill .				8 0 0
									Mar. 31	„ Joint Adventure Account—				1,073 0 0
										Share of Profit .				78 0 0
						£1,151	0	0						£1,151 0 0
Mar. 31	To Banker's draft from Brown . .					351	0	0	19..	Mar. 31	By Balance brought down . .			351 0 0

BROWN														
19..			£	s.	d.	£	s.	d.	19..			£	s.	d.
Feb. 1	To Joint Adventure								Jan. 1	By Bill (due Mar. 25th)		800	0	0
	Account—								" 20	" Joint Adventure				
	Timber sold		670	0	0					Account—				
" 17	" "		580	0	0					Dock dues, etc.		21	0	0
						1,250	0	0	Mar. 31	" Joint Adventure				
										Account—				
									Mar. 31	Share of Profit		78	0	0
										" Balance down		351	0	0
						£1,250	0	0				£1,250	0	0
19..									19..					
Mar. 31	To Balance brought								Mar. 31	By Banker's draft to				
	down					351	0	0		Smith		351	0	0

partnership by notice. He may, however, with the consent of the general partners, assign his share in the partnership, his assignee thereby becoming a limited partner in his place. A body corporate may be a limited partner.

A limited partner cannot take any part in the management of the business, beyond, by himself or his agent, inspecting the books of the firm, and examining into the state and prospects of the business, and advising with his other partners thereon. If he does take part in the management, he will be liable for all debts and obligations of the firm contracted during the period when he so acted.

A limited partnership is not dissolved by the death or bankruptcy of a limited partner, or by his charging his share in the partnership for his separate debt.

In the event of a dissolution of a limited partnership, the affairs will be wound up by the general partners, unless the Court otherwise orders. The Court has power, on a petition, to order a winding up not as formerly under the Companies Consolidation Act, 1908, but the winding up will be conducted in accordance with the provisions of

the law of Bankruptcy, and the rules relating to Bankruptcy as laid down in the Bankruptcy and Deeds of Arrangement Act, 1913, Section 24.

Every limited partnership must be registered with the Registrar of Joint Stock Companies, and a statement must be furnished containing the following particulars—

- (a) The firm's name,
- (b) The general nature of the business,
- (c) The principal place of business,
- (d) The full name of each of the partners,
- (e) The term—if any—for which the partnership is entered into, and the date of its commencement,
- (f) A statement that the partnership is limited, and the description of every limited partner as such,
- (g) The sum contributed by each limited partner, and whether paid in cash or how otherwise.

And, if during the continuance of a limited partnership, any change is made or occurs in—

- (a) The firm's name,
- (b) The general nature of the business,
- (c) The principal place of business,

- (d) The partners or name of any partner,
- (e) The terming or character of the partnership,
- (f) The sum contributed by a limited partner,
- (g) The liability of any partner by reason of his becoming a limited instead of a general partner, or a general instead of a limited partner,

a statement signed by the firm specifying the nature of the change, must be furnished to the Registrar of Joint Stock Companies.

The original statement must bear an *ad valorem* stamp of 5s. per £100 or fraction thereof on the amount contributed by a limited partner, and a similar duty on any increase thereof.

The original registration is subject also to a registration fee of £2, and in case of any change notified, a fee of 5s. is payable.

If any partner cease to be a general partner, and become a limited partner in a firm, or if the share of a limited partner be assigned to any person, it must be advertised in the *Gazette*.

A limited partner, for his own protection, should see that the original registration is effected, but the duty of registering any change is cast upon the general partners, who, in default, are each liable to a fine not exceeding £1 for each day during which the default continues.

As regards the accounts, the Capital Account of a limited partner should state that he is a limited partner, and will be credited with the amount which he contributes. This account should remain intact, except for any alteration in the amount of his contribution, and his other dealings with the firm should be recorded in his Current Account.

In case the trading results in a loss, the limited partner's share of that loss may be debited to his Current Account, but in the event of a dissolution, such losses could not be recovered from the limited partner, as he has contributed to the business the amount that he agreed to contribute.

These losses would therefore fall upon the general partners, and would have to be charged to them in the proportion in which they share profits.

Where losses have been debited to a limited partner's Current Account, he would not be entitled to withdraw anything until such losses had been recouped out of subsequent profits. In cases where amounts are drawn on account of profits, any amount so drawn by a limited partner, should be debited to his Current Account. If his share of the profits be not sufficient to counterbalance these, or if the business result in a loss, the total amount of such withdrawals, or such amount as is not counterbalanced by profits, would constitute a withdrawal of capital, and the limited partner would be liable to refund such amount in the case of dissolution.

INCOME TAX IN RELATION TO PARTNERSHIP.—In dealing with income tax in connection with partnership, it must be borne in mind that since the passing of the Finance Act, 1907, the profits of the individual partners in a firm are assessed through the firm. The firm pays tax on the income of its partners, so far as such income is derived from the business carried on by the firm, subject to any abatements and allowances to which they may be entitled individually.

This is in contradistinction to the former practice, under which the individual partners were entitled to claim to be assessed separately as regards their respective shares in the profits of the firm.

Under the present circumstances, therefore, it is necessary, where a claim is made for abatement, relief in respect of earned income or allowance, for each partner to render a separate statement showing his total income from all sources.

Any abatement, relief, or allowance to which a partner may be entitled, will be deducted from the gross assessment of the firm.

In dealing with income tax in the accounts of the firm, it is therefore necessary to allocate it to the partners, not in the proportions in which they share profits, but so as to give effect to the abatements and allowances, if any, to which they are respectively entitled.

Even in cases where no claim is made for abatement, the tax will require to be specifically dealt with, where the partners receive interest on their capital, or where some of them receive salaries.

The following are some of the principal points which have to be borne in mind—

So far as partnership accounts are concerned, the income tax schedules which are likely to affect them, are Schedule A and Schedule D.

Schedule A is to be considered where the firm owns the premises which it occupies, or where, if it does not own them, the amount of the rent paid is less than the Schedule A assessment of the property.

In ascertaining the average profits under Schedule D in these cases, Schedule A assessment will be deducted (after writing back any rent paid).

In arriving at the total income of each individual partner, it will be necessary to include their proportions of the Schedule A assessment, or the difference between Schedule A assessment and the rent paid, as the case may be.

The following is an example showing how the assessment of a firm is dealt with—

A, B, C, and D are in partnership as solicitors. Their capitals in the business (on which they are entitled to interest at 5 per cent. per annum) are—

A	£10,000	B	£5,000
C	£4,000	D	£1,000

They share profits—A $\frac{7}{16}$; B $\frac{5}{16}$; C $\frac{3}{16}$; D $\frac{1}{16}$.

D has a salary of £250 per annum.

The assessable profits of the firm under Schedule D as agreed with the Inspector of Taxes for the year are £3,650.

In order to ascertain the proportions chargeable to the respective partners, this amount must be divided between them on the same basis as that in which they divide the profits of each year thus—

	A	B	C	D
Salary				£250
Interest on Capital	£500	£250	£200	50
Share of Profits	1,050	750	450	150
Totals	£1,550	£1,000	£650	£450

To enable the partners to obtain whatever relief, abatement, or allowance they may be entitled to, each of them must make a return showing his total income from all sources.

In this case the income of the partners from other sources (tax paid) was—

A £1,600 B £1,200 C £500 D nil

They paid Life Assurance premiums as follows—

A £200 B £100 C £100 D £50

D has two children under the age of 16 at the commencement of the year of assessment.

Presuming that the partners had made their separate returns the following would be the position—

	A	B	C	D
Income from business	£1,550	£1,000	£650	£450
Income from other sources, all tax paid	£1,600	£1,200	£500	nil
Total income from all sources	£3,150	£2,200	£1,150	£450

A will be entitled to allowance of one-tenth of his earned income, say, £155, and, assuming that he is married, he will be entitled to a marriage allowance of £225, his remaining income will be taxed as to the first £225 at 3s. in the £, and as to the remainder at 6s. in the £, subject to the allowance for life assurance premiums, at, say, 6s. in the £. Therefore, the net assessment on the firm in respect of his share will be £257 5s.

B's allowances will be one-tenth of his earned income, £100, and the allowance to a married taxpayer of £225. His taxable income will be charged at 3s. in the £, and the remainder at 6s. Deduction for life assurance premium will have to be made, say, £100 at 4s. 6d. The assessment on the firm in respect of his share will thus be £146 5s.

C will deduct one-tenth of his earned income, and, assuming him to be an unmarried man, the personal allowance of £135. The remaining income will be taxable at 3s. in the £ on £225 and the remainder at 6s. in the £, from which will be deducted the insurance allowance, say, £100 at 3s.

The assessment on the firm in respect of C's share will be £86 5s.

D's allowances will consist of one-tenth of his earned income, marriage allowance £225, children's allowance £63. The remainder will be taxable at 3s. in the £, namely, £17 11s., less life assurance premium allowance £50 at 3s.

The firm will therefore receive an assessment notice as follows—

Schedule D. Profits		£3,650	£	s.	d.
Less Allowances—					
Earned Income					
A	£155				
B	100				
C	65				
D	45				
	£365				
Personal Allowance					
A	225				
B	225				
C	135				
D	225				
	810				
Children Allowance					
D	63	63			
		1,238			
		2,412			
Taxable £792 at 3s.		£118 16 0			
£1,620 at 6s.		486 0 0			
			604	16	0
Less Insurance Allowance—					
A £200 at 6s.	£60 0 0				
B 100 at 4s. 6d.	22 10 0				
C 100 at 3s.	15 0 0				
D 50 at 3s.	7 10 0				
			105	0	0
			£499	16	0

(See also AUDITING, p. 110; INCOME TAX, p. 945; INVESTIGATIONS, p. 581.)

PARTNERSHIP AGREEMENT.

(See INVESTIGATIONS, p. 583; PARTNERSHIP ACCOUNTS, p. 737.)

PARTNERSHIP, ARTICLES OF.

Partnership is a contract of a consensual nature, that is, it is formed by consent alone, and no special formality is required in establishing the same. It is very rare, however, for the contract to be made in this manner. The common practice is for all the terms to be embodied in a written agreement or a deed, and the document thus prepared is styled the "Articles of Partnership." These articles require the most careful preparation, and, as everything must depend upon the special circumstances of the business, the different experiences of the parties, the amount of capital to be provided by each, the supervision to be undertaken, and a host of other things of a similar character, no general rules can be given for guidance. Precedents should be consulted, and variations made in them in accordance with the requirements of the individual cases. The articles bind the partners as between themselves, but they have no binding authority upon the outside world,

except as far as those persons are concerned who are cognisant of their contents. They differ, in this respect, from the Articles of Association of a joint stock company which are common property and which any person who had business relations with the company must be assumed to be acquainted with. Since they are made by the mutual consent of the parties, the articles may be varied at any time if all the parties agree to the same. (See also AUDITING, p. 110; PARTNERSHIP ACCOUNTS, p. 737.)

PARTNERSHIP, CHANGE IN.

(See PARTNERSHIP ACCOUNTS, p. 759.)

PARTNERSHIP, DISSOLUTION

OF. (See PARTNERSHIP ACCOUNTS, p. 747.)

PARTNERSHIPS, LIMITED.

(See AUDITING, p. 113; PARTNERSHIP ACCOUNTS, p. 768.)

PARTY WALL.

Various definitions are given of this expression, and the following are a selection from them: A party wall is a wall between two buildings or pieces of land intended for distinct occupation, in the use of which each occupier has a partial right; a wall in which adjoining owners are tenants in common; a wall divided longitudinally into two strips, one belonging to each of the adjoining owners; a wall wholly belonging to one owner, but in which the neighbour has a right (easement of support); a wall divided longitudinally, and owned separately, but each owner possessing a right of support in his neighbour's half (cross easements).

Wherever there is a wall in existence the sole ownership of which is not vested in one person, difficulties are bound to arise occasionally upon the question of support, keeping in order, repair, etc. As far as possible, these difficulties are met outside the metropolitan area by means of by-laws passed by the various councils, whilst in London the London Building Act, 1894, is the main guide upon all such matters. To these by-laws and to the statute just named the reader must turn for guidance as to the rights and liabilities which attach to the owners of party walls.

PASS BOOKS, BUILDING

SOCIETY. (See AUDITING, p. 101.)

PASSIVE DEBT.

A debt upon which no interest is payable by arrangement between debtor and creditor, as distinguished from an active debt upon which interest is payable.

PASSIVE TRUSTS.

Trusts to which no duties are attached. A trust of this kind was originally created under the Statute of Uses to escape the hardships entailed

under the rules of the common law. Other instances of passive trusts are those created to preserve contingent remainders and to prevent dowry. In each of these cases there is absolutely nothing for the trustee to do. If a trustee has any duty whatever to perform the trust is called an "active trust."

PATENTS AND MODELS.

(See MODELS AND PATENTS.)

PATENTS, TRADE-MARKS, ETC.

(See ACCOUNTS, CRITICISM OF, p. 18; DEPRECIATION, p. 412; RENEWALS AND DEPRECIATION.)

PATTERNS AND DRAWINGS.

In many cases the intrinsic value and residual value of patterns and drawings is comparatively small, and in such cases it is advisable that they should be regarded as revenue charges and treated as such.

Where there has been a considerable expenditure upon these subjects and an exceptional value attaches to them because of the use to which they are put, they may be temporarily capitalised. In any case, however, they are assets which very quickly wear out and have little residual value. The rate of depreciation which should be applied to them is, therefore, a heavy one. They should be extinguished certainly within not less than three or four years. If they are not likely to be used for more than a single season, the whole cost should be charged against the current period's revenue.

The auditor should assure himself of their existence by having a duly vouched inventory produced to him, and should satisfy himself that an adequate provision has been made for the loss in value by depreciation.

PAWN OR PLEDGE.

This is the delivery of the possession of goods or of documents of title to goods by one person to another as a security for a debt. The person to whom the goods are delivered is entitled to retain them so long as the debt is outstanding, and, if the due date of repayment passes by, to sell the same and reimburse himself, handing over any balance that remains to the pledgor. If, on the other hand, the sale does not realise sufficient to cover the amount of the debt, the pledgee can sue the pledgor for the difference. It will be at once obvious how a pawn or pledge differs from a lien (*q.v.*). So long as the goods remain in the possession of the pledgee, he must exercise all reasonable care with regard to them, otherwise he will be liable to the owner. Moreover, he must not make use of them if they are liable to deterioration by usage.

Special rules apply to pawnbrokers, who are persons licensed to carry on the business of taking goods and chattels in pawn. The rights and the

liabilities of pawnbrokers are provided for by the Pawnbrokers Act, 1872. The principal of these are as follows—

(1) The Act does not apply to loans of more than £10.

(2) The pledge must be authenticated by a pawn-ticket.

(3) Every pledge may be redeemed at any time before sale, except that where the amount lent is not more than 10s. the pledge becomes the absolute property of the pawnbroker after twelve months and seven days.

(4) If the loan exceed 10s. the pledge must be sold by auction. Any balance, after the expenses of the sale, the loan, and the interest have been paid, belongs to the pledgor, who is, in turn, liable to be sued for any deficiency.

(5) Special contracts may be entered into when the amount of the loan exceeds 40s., and must be authenticated by special pawn-tickets signed in duplicate.

The rate of interest which a pawnbroker is entitled to charge is—

(a) On pledges for sums not exceeding 10s., one halfpenny for every month or part of a month on each 2s., and a halfpenny for the ticket.

(b) On pledges for sums between 10s. and 40s., the same rate as before, and one penny for the ticket.

(c) On pledges for sums between 40s. and £10, one halfpenny for every month or part of a month on each 2s. 6d., and one penny for the ticket.

As a pawnbroker is liable for loss by fire, it is his duty to protect himself by insurance.

A pawnbroker must make all reasonable inquiries as to goods which he takes in pledge, otherwise he may be a heavy loser. If, for example, he takes in goods which have been stolen, he must restore them to the rightful owner on demand, and under ordinary circumstances he is not entitled to anything in the way of compensation. On the other hand, when the pawnbroker sells, he does not confer any better title than he himself possessed, in the absence of any special warranty to that effect or of fraud, and even though the purchaser may be compelled eventually to give up the goods sold to him, if they have been stolen, to the rightful owner, the purchaser has no right to claim back his purchase money from the pawnbroker.

When a pawn-ticket is lost or mislaid, the pledgor should apply to the nearest police magistrate for relief, as the pawnbroker is bound *primâ facie*, to deliver up the goods pledged to the person who presents the ticket and offers to repay the amount advanced, with the interest that is due.

PAYEE, ALTERNATIVE.

(See ALTERNATIVE PAYEE.)

PAYEE OF BILL OF EXCHANGE.

(See BILL OF EXCHANGE, PAYEE.)

PAYMENT FOR HONOUR, BILL OF EXCHANGE.

(See BILL OF EXCHANGE, PAYMENT FOR HONOUR.

PAYMENTS.

(See AUDITING, p. 74.)

PENDING CONTRACTS.

(See BANKRUPTCY ACCOUNTS, p. 161.)

PENSION FUND ACCOUNT.

Contributions to a Pension Fund are debited to the Profit and Loss Account and credited to the fund. Payments to the pensioners are then debited against the fund, the balance of which appears amongst the liabilities in the Balance Sheet.

In the case of a public company, the contributions to the fund must be supported by resolutions of the directors or the shareholders, as the case may require. The auditor should ascertain that the creation of the fund is *inter vires* the directors or the company.

The pensions paid will be vouched by the production of the pensioners' receipts. Additional pensions granted from time to time will be verified by reference to the minutes. In addition to this, it is advisable to have a schedule of the pensions paid, made out and certified by a responsible official, and for the directors to pass a minute authorising or confirming the payments. (See ANNUITIES TO EMPLOYEES.)

PEPPERCORN RENT.

This is the name which is given to a rent of merely nominal value, pecuniary or otherwise. When the owner of an estate wishes to develop it, by building or otherwise, he is generally willing to lease it to a lessee, who is anxious to undertake the work of development, provided that, during the time that he is so developing it, the lessee is not called upon to pay more than a nominal rent for the land itself. Thus, A is the owner of an estate. He leases it to B, who is anxious to build upon it. For some time it is obvious that B can get no real advantage out of the estate, indeed, he can hope for nothing until the buildings are completed. During the time that the work is going on, A agrees to accept a merely nominal rent. This is called a peppercorn rent, because at one time it was the custom to fix the rent at a peppercorn, if demanded.

PER CAPITA (by the heads).

This means that, where a man dies leaving children, they share his personal estate between them. (See also EXECUTORSHIP ACCOUNTS, p. 448.)

PERCENTAGE STATEMENTS AS APPLIED TO ACCOUNTS.

Percentage statements form important aids to the interpretation of financial accounts and to the

comparison of the costs and results of one period with another.

When the figures in the accounts are shown in the form of percentages upon the sales, any leakages or excess expenses are at once thrown into relief if brought into line with the percentages of previous periods. The leakages might escape notice if the accounts only are compared, but by the reduction of the items to a common denominator—preferably the sales—variations are easily detected. It may be safely asserted that a Trading Account, unsupported by a percentage statement, does not supply the trader with information sufficiently helpful to enable him to detect speedily growing waste or leakage.

It is customary for a Trading Account to be drawn up in sections, the balance of Section 1 being usually the gross profit on the sales. A business man knows the approximate percentage of gross profit which his sales should realise, and to make his Trading Account complete, he would require to state the percentage actually realised on the sales as shown in the Trading Account.

If this percentage is not in accordance with what he has been expecting, he will at once look into matters so as to adjust the difference. A drop in the percentage of gross profit would point to—

- (a) declining sales ;
- (b) increased cost of goods or advance in wages ;
- or
- (c) loss or depreciation of stock.

In addition to the periodical Trading Account giving details of the revenue and expenses of a business, there should be, either as an additional statement or incorporated in the Trading Account, a table showing the percentage which the various items of expense bear to the sales.

The percentages may be with respect to every item appearing in the Trading Account, or only with respect to groups of items. Where every item is shown as a percentage of the sales, it is usually done by ruling an additional column in the Trading Account so as to enter not only the amounts for the period, but also the percentages.

If a grouped statement is required, the following summary may meet the case—

Materials used	—%	on sales.
Wages (production)	—%	„
Prime Cost	—%	„
Distributive Expenses	—%	„
Administrative Expenses	—%	„
Financial Expenses	—%	„
Total Cost	—%	„
Net Profit	—%	„
Sales	100%	„

To obtain the percentage which any item bears to the sales, multiply the item by 100 and divide the product by the total of the sales. Every table of percentages should be drawn up so as to show the percentages for the last three periods, if possible, in order that an easy comparison may be obtained. The periods should be given in separate columns, thus—

	1920.	1921.	1922.
	%.	%.	%.
Materials used	48·63	49·73	48·41
Wages (productive) ..	35·61	32·14	33·30
Prime Cost	84·24	81·87	81·71
Expenses	8·37	9·92	7·64
Total Cost	92·61	91·79	89·35
Net Profit	7·39	8·21	10·65
Sales	100·00	100·00	100·00

Another form of comparative statement showing the percentages which various groups bear to the sales is shown below.

In some undertakings the basis adopted is the prime cost and not the sales. The percentage

	1920.		1921.		1922.	
	Amount.	Of Sales.	Amount.	Of Sales.	Amount.	Of Sales.
	£	%.	£	%.	£	%.
Cost of Production ..	13,500	67·50	12,000	61·54	15,000	68·18
Cost of Distribution ..	1,000	5·00	800	4·10	1,200	5·45
General Expenses ..	500	2·50	600	3·08	650	2·96
Total Cost	15,000	75·00	13,400	68·72	16,850	76·59
Net Profit	5,000	25·00	6,100	31·28	5,150	23·41
Sales	20,000	100·00	19,500	100·00	22,000	100·00

	1920.		1921.		1922.	
	Amount.	On Prime Cost.	Amount.	On Prime Cost.	Amount.	On Prime Cost.
	£	%.	£	%.	£	%.
Materials used ..	6,500	48·15	6,200	51·67	7,800	52·00
Labour	7,000	51·85	5,800	48·33	7,200	48·00
Prime Cost	13,500	100·00	12,000	100·00	15,000	100·00
General Expenses ..	1,500	11·11	1,400	11·66	1,850	12·33
Total Cost	15,000	111·11	13,400	111·66	16,850	112·33
Net Profit	5,000	37·03	6,100	50·84	5,150	34·33
Sales	20,000	148·14	19,500	162·50	22,000	146·66

statement would, when calculated upon the prime cost, be shown as above.

These comparative percentage statements furnish valuable information to the management, particularly if the business is one where the work is not of a varying character and where it is mostly contracted for. The table showing the percentages calculated upon the prime cost tells one that the General Expenses (which include the factory on-cost) run out at about 12 per cent. on the prime cost. Consequently, when estimating for future work, the management would calculate the materials and labour necessary to complete the job, and to that total would add 12 per cent. to cover expenses and a further percentage to cover profit, and lodge a quotation accordingly. Or the past estimates could be compared with the percentages shown in the actual statement and past errors in estimates avoided in the future.

These percentage statements are a guide also in the profitable expansion of trade. There is a point in production beyond which the cost would be such as to reduce instead of increase profits. That margin of output is the extreme paying capabilities of the business, and to tax the powers of the business beyond that would mean additional expense out of proportion to the extra work done. This is brought out in the percentage statement by a decreased percentage of gross profit upon a turnover which is increasing.

Again, the percentage of wages upon the turnover is, in many businesses, known to be a certain figure, say 33·5 per cent., and beyond that figure a loss or leakage may be taking place. If the comparative percentage statement shows the wages to have been 35 per cent. upon the turnover, the management will investigate to see whether there are too many hands employed for the amount of work turned out. It may be found that the wage list contains "dead men"—that is, fictitious names, the pay clerk misappropriating the amount entered as the wages earned by these—and the

rise in the percentage thereby explained, and a stop put to the leakage. (See also FRAUD AND FALSIFICATION OF ACCOUNTS.)

PERMANENT BUILDING SOCIETY.

(See BUILDING SOCIETIES.)

PERMANENT CAPITAL.

(See ACCOUNTS, CRITICISM OF, p 19.)

PERPETUITY.

In order to prevent property being tied up indefinitely, so that it may not be dealt with by some person in possession, there are certain rules of law laid down which limit the period during which it can be thus tied up, and these are known as the rules against perpetuity. Under these rules an executory interest in property of any kind, real or personal, cannot be created so as to take effect unless within the period of a life or lives in being and twenty-one years afterwards, with an allowance for the period of gestation, if, in fact, gestation actually exists. If the period allowed is exceeded, the settlement is wholly void.

Until the year 1800 property could be tied up for the period or periods named, whether any profits were payable out of it or whether it was left to accumulate at compound interest. A remarkable will of a Mr. Thellusson caused the passing of a special Act in the year just named, by which the period of accumulation was strictly limited, the object being to prevent enormous wealth getting into the possession of one single individual at a distant date. By the Thellusson Act, the accumulation of income in the manner just stated can only be directed (1) during the life of the settlor and twenty-one years after; or (2) during the minority or minorities of a person or persons living at the time of the death of the settlor; or (3) during the minority or respective minorities of a person or persons who, if of full

age, would have been absolutely entitled under the settlement. There are certain exceptions as to provisions for paying debts and providing portions for children. If an accumulation is directed for a period extending beyond what the law allows, the direction is not void, but the excess goes to the person who would have been entitled to the property if there had been no accumulation directed. This Act was at first only applicable to England and Wales. It was extended, by a special Act, to Scotland in 1848. By a further Act, passed in 1892, where money is directed to be accumulated for the purchase of land, such accumulation is only permissible during the period mentioned in (3) above.

PER PROCURATION.

This is the common way of using the two Latin words *per procuracionem*, abbreviated as *per pro.* or *p.p.*, and the meaning of the phrase is that an agent signing a document with *per pro.*, or *p.p.* written before his name, holds out to the world that he has authority to sign on behalf of the principal named. An agent is not personally liable if he signs for, or on behalf of, his principal, and clearly indicates that he is only acting in a representative capacity. But if the agent simply adds words of description to his name, he will not escape liability. Thus, if A B signs "*Per pro.* C D Limited, A B," he is not liable; but if he signs, "A B, agent for C D Limited," he is liable.

When an agent signs *per procuracionem*, it is essential that the other party to the contract should ascertain the extent of the agent's authority, especially when it is a question of a bill of exchange, for by the Bills of Exchange Act, 1882, it is provided, in the 25th section—

"A signature by procuracion operates as notice that the agent has but a limited authority to sign, and the principal is only bound by such signature if the agent in so signing was acting within the actual limits of his authority."

PER SALTUM.

This is applied to a grant of letters of administration over the head of one who may have a prior right, (See also EXECUTORSHIP ACCOUNTS, p. 448.)

PERSON.

In a legal sense, the word person is applicable to any individual—male or female—or to any aggregate of individuals to whom or with reference to whom certain rights or liabilities attach.

PERSONAL ACCOUNTS.

Personal Accounts are those by which the accounts of persons who are dealt with are kept, and are of two classes, namely, Debtors' Accounts and Creditors' Accounts. A Personal Account which contains the transactions of a person in the capacity of both debtor and creditor is known as a "Contra Account." Debtors' Accounts are assets, and Creditors' Accounts are liabilities, and as such appear in the balance sheet.

The accounts of persons with whom trade is done are kept in the Personal (Debit and Credit) Ledgers, but those of persons to whom money is lent, or from whom it is borrowed, are usually kept in the Private Ledger. The Cash and Bank Accounts are also, strictly speaking, Personal Accounts with the Cashier and the Banker, respectively. (See below.)

PERSONAL ACTION.

An action against a person, or action *in personam* which settles the question in dispute as to a particular individual and fixes his liability. It is to be distinguished from a real action (*q.v.*) which affects the right in the property of a certain thing as against the whole world.

PERSONAL LEDGER.

The Ledger containing the accounts of persons with whom business is done, comprising both ordinary trade creditors and trade debtors.

PERSONAL PROPERTY.

One of the principal divisions of property is into real and personal. The latter consists of such things as money, goods, furniture, stocks and shares, etc. Leasehold property, even a lease for 999 or any other number of years, is personal estate, or, to use its proper technical name, personalty. Also when real estate (*q.v.*) is directed by will to be sold, it is regarded as

PERSONAL ACCOUNT											
Dr.			J. JONES						Cr.		
19..			£	s.	d.	19..			£	s.	d.
Feb. 5	To Goods		15	12	6	Mar. 9	By Returns		2	3	3
" 14	" "		29	4	9	" "	" Cash		41	2	6
" 26	" "		48	6	4	" "	" Discount		1	11	6
						" "	" Balance c/d		48	6	4
			£93	3	7				£93	3	7
19..											
Mar. 9	To Balance b/d		48	6	4						

personalty, and so is the benefit of a mortgage. When personalty is dealt with in a will, the property is "bequeathed," and the person to whom it is given is called the "legatee." In the case of realty, the property is "devised," and the beneficiary is the "devisee."

PERSONALTY.

(See EXECUTORSHIP ACCOUNTS, p. 448; PERSONAL PROPERTY.)

PER STIRPES (by the stem).

This means that, where a man dies leaving children and children of a deceased child, the children of the deceased child take their parent's share between them. (See also EXECUTORSHIP ACCOUNTS, p. 448.)

PETITION, BANKRUPTCY.

(See BANKRUPTCY PETITION.)

PETTY CASH.

The cash utilised for small payments, such as postages, tram and railway fares, small cash purchases, cleaning, and incidental expenses, is known as Petty Cash; it is important that these items be carefully recorded and find their way to the respective Nominal Accounts.

Not being of sufficient magnitude to be dealt with separately, they should be kept in a special book for the purpose, the matter usually being placed in the hands of a person subordinate to the cashier.

In small firms the only method of treatment is to enter them up as they take place, the total of the book at any moment being part of the cash expenditure, which must be taken account of in balancing the cash, the book being totalled and analysed and the posting made through the Cash Book periodically. In this case the Petty Cash Book should be as shown in the opposite column.

A much better method, however, is to adopt the system known as the Imprest System (*q.v.*) and a better form of Petty Cash Book provides for the analysis as the expenditure takes place, the specimen shown on page 778 being adapted to meet the requirements of the Imprest System. (See also INVESTIGATIONS, p. 586; SELF-BALANCING LEDGERS, p. 850.)

PLANT.

(See AUDITING, p. 96; LIQUIDATORS, ACCOUNTS OF, p. 648; RENEWALS AND DEPRECIATION.)

PLANT AND MACHINERY.

(See AUDITING, p. 92; BALANCE SHEET, p. 144; BOOK VALUES.)

Dr.			PETTY CASH BOOK.		Cr.		
£	s.	d.	19..	TOTAL.	£	s.	d.
40	0	0	Dec. 1	To Cheque			
			" "	By Stamps	2	0	0
			" "	" Office Cleaner		5	0
			" "	" Telegram (F. Davies)		1	6
			" "	" Repairs (Plumber)	10	6	
			" 2	" Stationery	12	0	
			" "	" Telegram (J. Brown)		1	8
			" "	" Office Stool	12	0	
			" "	" Fare (Manchester)	16	0	
			" 3	" Stamps	12	0	
			" "	" Trunk Calls		4	6
			" "	" Packing Materials	10	0	
			" 4	" Carrier	1	2	6
			" "	" Window Cleaner		5	0
			" "	" Pens and Pencils		6	0
			" "	" Directory	1	1	0
			" 5	" Wages, Two Casual Men, three days at 5s. per day each	1	10	0
			" "	" Telegram (J. Webb)		1	3
			" "	" Repairs (Electrician)	15	2	6
			" 6	" Stamps	2	15	0
			" "	" Office Desk	4	15	0
			" "	" Telegrams—			
			" "	W. Boyd		1	6
			" "	H. Jackson		1	9
			" "	F. Welsh		1	3
			" "	" Stationery	12	6	
			" "	" Fare (Chiswick)		4	0
			" "	" L. & N.W. Railway	10	0	
			" "	" L.B. & S.C. Railway	2	15	0
					37	9	5
				" Balance c/d	2	10	7
40	0	0			40	0	0

SUMMARY

	£	s.	d.
Postage	5	7	0
Telephone and Telegrams		13	5
Carriage	4	7	6
Office Expenses		10	0
Stationery	1	10	6
Travelling	1	0	0
Repairs	15	13	0
Sundries	3	1	0
Fixtures and Fittings	5	7	0
	£37	9	5

PLANT AND MACHINERY, ADDITIONS TO.

The sums charged to Plant and Machinery Account in respect of additions thereto, should be carefully scrutinised by the auditor. He should satisfy himself, as far as possible, that such additions are legitimate capital expenditure. In cases of doubt he may even go so far as to inspect the reputed additions himself, though this extreme step should be rarely necessary. In any event he should require upon each invoice, the contents of which are allocated to capital, the certificate of the engineer that the expenditure

is a proper capital addition, and not merely a part of the cost of the upkeep of the plant and machinery. The certificate should be supported by some other responsible person, preferably the managing director, or other director. The auditor should further see that a resolution authorising the additions to the Plant and Machinery Account is properly recorded upon the minutes of the directors' meetings.

PLANT AND MACHINERY : DEPRECIATION OF.

(See DEPRECIATION, p. 405.)

PLEDGE.

(See PAWN OR PLEDGE.)

POLICIES, CLAIMS UNDER.

(See AUDITING, p. 79.)

POSSESSION, ADVERSE.

(See ADVERSE POSSESSION.)

POST-NUPTIAL SETTLEMENT.

This is the name given to a settlement which is made after marriage. Marriage is a valuable consideration in law; and, unless the circumstances are connected with fraud, an ante-nuptial settlement is always valid against the trustee in bankruptcy, provided the settlement is not for the future payment for the wife, husband, or children, under Section 42, Subsection 3 (c) of the Bankruptcy Act, 1914. But if the settlement is a post-nuptial one, that is, made after marriage, it is no other than a voluntary settlement, and although binding upon the parties themselves, is void against the trustee in bankruptcy, if the bankruptcy takes place within two years of the date of the settlement, and also if the bankruptcy takes place within ten years of the date of the settlement, unless it is proved that the settlor was able, when the settlement was executed, to pay the whole of his debts without the aid of the property comprised in the settlement. After ten years a voluntary settlement is just as secure in bankruptcy proceedings as a settlement which is supported by a valuable consideration. (See VOLUNTARY SETTLEMENT.)

POST OBIT BOND.

A bond in which a person, for a present pecuniary consideration, undertakes to pay a certain sum of money after the death of some particular individual from whom the borrower has financial expectations. A bond of this kind is not illegal, provided the borrower is a person of contractual capacity; but if there be any fraud, duress, or bargain of an unconscionable character, the Court will inquire into the whole transaction, and make such order as to repayment or otherwise as it thinks just under all the circumstances.

POSTING.

The entry of the records made in the books of first entry to their appropriate accounts in the Ledgers. (See also SLIP SYSTEM OF POSTING.)

POSTPONED CREDITORS.

These are the creditors in bankruptcy whose claims are not admitted for the purpose of ranking for dividend until other creditors have been fully satisfied. (See BANKRUPTCY, DEFERRED DEBTS IN).

POWER OF APPOINTMENT.

This is a right which is granted to a person or persons under a deed or will empowering him or them to deal with the property comprised in that deed or will. It arises, however, most commonly in the case of a marriage settlement where life interests are given first of all to the husband and wife, with remainder either to any children of the marriage or to other specified individuals or classes of individuals, but the proportion in which these latter are to take is made to depend upon the exercise of a power of appointment given under the marriage settlement either to the husband or to the wife, or to the two jointly. It is most essential that when a power of appointment is given the document conferring it should be most carefully studied in order to ascertain that the right or rights granted to the appointor or appointors are strictly carried out. No person upon whom a power of appointment is conferred may make use of it in such a manner as to obtain some private advantage for himself. Such an act will render the appointment void as a fraud upon the power.

POWER OF ATTORNEY.

This is a formal document under which one person is empowered to act for and on behalf of another. It is drawn up in the form of a deed, and, as such, requires a 10s. stamp.

Although it is open for any person to appoint an attorney upon any occasion or for any purpose, a document of this character is most commonly resorted to when the grantor of the power is going abroad and desires the attorney to act for him during his absence as his special agent. It is a part of the law of agency that the authority of the agent is determined by the death or insanity (*inter alia*) of the grantor. This might easily lead to very serious complications when the fact of the death or insanity was unknown to the attorney or to other persons at the time of carrying out some transaction under the power. To prevent difficulties arising out of acts done by an attorney in the name of the grantor after the termination of his authority by operation of law, and without the knowledge of the attorney

and the person with whom the attorney is dealing, it has been enacted by Sections 8 and 9 of the Conveyancing Act, 1882, that any act done under a power of attorney will be permanently effectual in favour of the purchaser, if the power of attorney is given for valuable consideration and expressed to be irrevocable, and will be effectual for a fixed time, whether given for a valuable consideration or not, if the power is expressed to be irrevocable for a specified time, not exceeding one year, from the date of the instrument.

The following is a common form of a power of attorney, which is like a deed poll—

Know all men by these presents that I, A B, of etc., have made, ordained, constituted, and appointed, and by these presents do make, ordain, constitute, and appoint C D, of etc., to be my true and lawful attorney for me in my name and behalf to ask, demand, sue for, enforce payment of and receive and give effectual receipts and discharges for all moneys, securities for money, debts, legacies, goods, chattels, and personal estate, of or to which I am now or may hereafter become possessed of or entitled to, or which are or may become due, payable, or transferable to me from or by any person or persons whomsoever. And upon receipt of any moneys under or by virtue of these presents, to pay the same to or deposit the same with any banker, broker, or other person on my behalf, and to lay out or invest the same or any part thereof in such stocks, funds, shares, or securities as he my said attorney shall think fit. And for the purposes aforesaid, or any of them, to sign my name to, and make, execute, and do on my behalf any cheques, contracts, agreements, deeds, transfers, assignments, instruments, and things whatsoever. And generally to act in relation to my estate and effects as fully and effectually in all respects as I myself could do, I hereby undertaking to allow, ratify, and confirm everything which my said attorney shall do or suffer by virtue of these presents. And I declare that this power shall be irrevocable for twelve calendar months computed from the date hereof.

In witness whereof I have hereunto set my hand and seal this 1st day of June, 19..

Signed, sealed, and delivered by the above-named A B in the presence of . . .

The grantor signs and seals the power of attorney, which must be attested by two witnesses, who add their names and descriptions.

It has been mentioned above that the stamp required is an ordinary deed stamp of 10s. Certain powers of attorney, however, are less heavily taxed, namely—

	s. d.
Power to receive prize-money or wages	1 0
Power for sale, transfer, or acceptance of any of Government funds not exceeding £100	2 6

s. d.

Power for receipt of dividends or interest of any stock, if for one payment only	1 0
Power for same in any other case	5 0
Proxy to vote at a meeting	0 1

POWERS OF EXECUTORS AND ADMINISTRATORS.

(See EXECUTORS AND ADMINISTRATORS.)

PRECEPT.

The general meaning of this term is any order or direction given by a responsible person for the payment of a particular sum of money or the doing of a specified act. In its narrower sense the word is applied to denote the written warrant of a magistrate.

PRE-EMPTION.

A preferential option of purchase when any property is to be offered for sale. It occurs very frequently in partnership articles, where it is stipulated that upon the dissolution of the partnership the partner who is continuing the business shall have the right to purchase the interest of any outgoing partner or partners before the same is offered to any other person.

PREFERENCE.

The right of an executor to pay one creditor before another of the same degree. (See also EXECUTORSHIP ACCOUNTS.)

PREFERENCE SHARES.

(See SHARES, CLASSES OF.)

PREFERENCE SHARES, UNPAID DIVIDENDS ON.

(See AUDITING, p. 90.)

PREFERENTIAL CREDITORS.

Under the provisions of the law applicable in bankruptcy and in the winding up of joint stock companies, certain creditors are entitled to be paid their debts before other creditors can be admitted to enforce their claims. The rules as to these preferential claims may be summarised as follows, and the following are the payments which must be made before the other creditors are considered—

(a) All parochial or other local rates due from the bankrupt or the company at the date of the receiving order or the commencement of the winding-up, and having become due and payable within twelve months next before that time, and all assessed taxes, land tax, property or income tax assessed on the bankrupt or the company up to the fifth day of April next before the date of the receiving order, or the commencement of the winding up, and not exceeding in the whole one year's assessment.

(b) All wages or salary of any clerk or servant

in respect of services rendered to the bankrupt or the company during four months before the date of the receiving order, or the commencement of the winding up, not exceeding £50.

(c) All wages of any labourer or workman not exceeding £25, whether payable for time or piece work, in respect of services rendered to the bankrupt or the company during two months before the date of the receiving order or the commencement of the winding up; provided that where any labourer in husbandry has entered into a contract for the payment of a portion of his wages in a lump sum at the end of the year of hiring, he shall have priority in respect of the whole of such sum, or a part thereof, as the Court may decide to be due under the contract, proportionate to the time of service up to the date of the receiving order or the commencement of the winding up.

(d) All amounts (not exceeding in any individual case £100) due in respect of compensation under the Workmen's Compensation Acts.

(e) All contributions payable under the National Insurance Acts and the Unemployment Insurance Acts, in respect of the four months preceding the bankruptcy or winding up.

These debts rank equally between themselves, and must be paid in full, unless the assets of the bankrupt or the company are insufficient to meet them, in which case they must abate proportionately. The only other reduction to which they are liable is the sum necessary for the costs of administration, etc.

Although the landlord has a right to distrain for six months' rent accrued due before the date of the receiving order, his right is postponed to the above, and in that respect he cannot really be called a preferential creditor.

In any case, however, these claims of preferential creditors do not affect the prior claim for funeral and testamentary expenses, where it is the case of a person dying insolvent, and if the bankrupt has, at the commencement of his bankruptcy, any funds in his possession which have come to him in his character as the officer of a friendly society or of a savings bank, these funds cannot be used for paying the claims of the preferential creditors. The friendly society or the savings bank, as the case may be, is entitled to be paid the funds due to it before any other claim is provided for. (See also *BANKRUPTCY ACCOUNTS*, pp. 167 and 210; *CROWN DEBTS, LIQUIDATORS, ACCOUNTS OF*, pp. 653, 681.)

PRELIMINARY EXPENSES.

(See *AUDITING*, p. 95; *BALANCE SHEET*, p. 154; *LIMITED COMPANY ACCOUNTS*, p. 630; *PROFIT AND LOSS ACCOUNT*, p. 793.)

PREMISES.

In a deed, the premises comprise all that portion of the document which precedes the

habendum (*q.v.*), that is, the date, the names and description of the parties, the recitals, the consideration, the receipt for the consideration, the grant, the description of the things granted, and the exceptions. It is generally asserted that the common use of the word premises, as in the phrase "eligible premises," meaning desirable property connected with an interest in land, is derived from the frequency with which the word occurs in conveyances and leases of lands and houses. In pleadings and similar documents, the word is used in its logical sense, that is, to signify foregoing statements or previously mentioned facts. (See also *ALTERATIONS AND IMPROVEMENTS TO PREMISES*.)

PREMIUMS, APPRENTICE.

(See *APPRENTICE PREMIUMS*.)

PREMIUMS, INSURANCE.

(See *AUDITING*, p. 80; *PROFIT AND LOSS ACCOUNT*, p. 787.)

PREMIUMS ON SHARES.

(See *AUDITING*, p. 78; *BALANCE SHEET*, p. 142; *CAPITAL RECEIPTS*; *PROFIT AND LOSS ACCOUNT*, p. 788.)

PREPAID EXPENSES.

(See *ADJUSTMENTS AT BALANCING TIME*.)

PRESCRIPTION.

This is the name applied to the title which a person acquires in incorporeal hereditaments, that is, those matters connected with the soil which are not the actual possession in the land itself, by long and continued possession, just as by long adverse possession he may acquire a title to corporeal hereditaments under the Statutes of Limitations. The most common of these are rights of way, ancient lights, etc. It was a presumption of law that any right of this kind must have been acquired in the first instance by grant, but it was often difficult to prove the grant. There thus arose a fiction in law that if a person could prove that he had enjoyed a right in an incorporeal hereditament since the date of the accession of Richard I, that is, 1189, he possessed a title by prescription, which no one could interfere with; otherwise his claim might be defeated. By the Prescription Act, 1833, however, rights of the character named are held to be indefeasible if they have been enjoyed for a certain period without interruption. Thus, the right of light—ancient lights (*q.v.*)—is firmly established after an enjoyment of twenty years, and a right of way is absolutely indefeasible after sixty years, though it is extremely difficult to defeat such a right after a continuous enjoyment of forty years.

PRESENTMENT FOR ACCEPTANCE.

(See BILL OF EXCHANGE, PRESENTMENT FOR ACCEPTANCE.)

PRESENTMENT FOR PAYMENT.

(See BILL OF EXCHANGE, PRESENTMENT FOR PAYMENT.)

PREVENTION OF FRAUD.

(See FRAUD; FRAUD AND FALSIFICATION OF ACCOUNTS.)

PRICE LISTS.

(See CATALOGUES AND PRICE LISTS.)

PRIME COST.

(See COST ACCOUNTS, p. 353.)

PRINCIPLE, ERRORS OF.

(See AUDITING, p. 66.)

PRINTING AND STATIONERY.

The cost of printing and stationery is, through the medium of the Printing and Stationery Account, chargeable, as an expense of sale and distribution, against the Profit and Loss Account. Where large quantities of stationery have been purchased in advance, it is permissible for the unused portion to be taken into stock and to be credited in the account. The auditor should see, however, that it is not over-valued. It is a variety of stock which rapidly deteriorates by keeping and should be taken, therefore, at less than cost price. If possible, it is preferable to ignore its existence at stocktaking times.

The printing of advertising circulars and matter should be charged against the Advertising Account, and not included in Printing and Stationery Account.

The auditor should compare the charges for printing and stationery made against the Profit and Loss Account with those of previous periods, in order to ascertain that there is no undue leakage under this heading. In doing so, he should have regard to any heavy purchases of printed matter and stationery which, though unused, may have been excluded from the stock.

PRIORITY OF CHARGES.

(See PREFERENTIAL CREDITORS.)

PRIVATE AUDITS.

(See AUDITING, p. 54.)

PRIVATE LEDGER.

The Ledger in which are entered all matters of a private nature relating to a business, including the accounts for Capital, Drawings, Loans, Investments and Fixed Assets. Should it be desired to

preserve the privacy of the Bank Account, this also may be dealt with by inserting the totals from the Cash Book from time to time, the insertion of the total to date at any time completing the account and showing the position. The Profit and Loss Accounts and Balance Sheets are usually inserted in the Private Ledger, so providing ready reference to the results of past periods, and comparisons of such results. The Private Ledger should be fitted with a lock, care being taken that the keys are retained by those persons having the right to examine the book.

By raising a Private Ledger Adjustment Account, to which all transactions during the period which require posting to the Private Ledger are entered, a trial balance may be prepared at any time without reference to it, the balances from it taking the place of the balance of the Private Ledger Adjustment Account on completion. Thus, private information may be kept away from the staff without in any way delaying or interfering with their work.

PRIVATE LEDGER CONTROL ACCOUNT.

(See SELF-BALANCING LEDGERS, p. 854.)

PRIVATE LIMITED COMPANIES.

From the point of view of the auditor, the private company has little to distinguish it from the public company. It is necessary for every joint stock company under the Companies (Consolidation) Act, 1908, to appoint an auditor or auditors, and failure on the part of the company to carry out this statutory duty will throw on the Board of Trade the authority to make the appointment. In certain matters, however, the difference between a private and a public company will have its effect on the auditor. Previous to the passing of the Companies Act, 1907, the distinction was a commercial one rather than a legal one; but now a definition of a private company is to be found in Section 121 of the Companies (Consolidation) Act as amended by the Companies Act, 1913. The combined definition is as follows—

A private company is a company which by its articles:

(a) Restricts the right to transfer its shares and

(b) Limits the number of its members (exclusive of persons who are in the employment of the company, and of persons who, having been formerly in the employment of the company, were, while in such employment and have continued after the determination of such employment, to be members of the company) to fifty; and

(c) Prohibits any invitation to the public to subscribe for any shares or debentures of the company.

It should be noted that the definition merely requires that the company shall by its articles make the above provision. Doubts were raised as to what effect would be produced if, in spite of provision in the articles, the board and the members of the company ignored the conditions. To prevent difficulties of this kind the Companies Act, 1913, was passed; and now, where a private company makes default in complying with those provisions of its articles which give it the privileges of a private company, it shall cease to be entitled to the privileges and exemptions conferred on private companies and mentioned in the schedule to the Act. Thus a private company offering its shares to the public would lose—

1. The right to be exempt from filing a statement in the form of a balance sheet as part of its annual list and summary;

2. The right to a minimum limit of two members; and

3. The right to be exempt from sending to shareholders and debenture holders copies of balance sheet and report.

The effect of failure on the part of a private company to observe the condition of its articles is not to convert such company into a public one. This can be done, however, by the company passing a special resolution and filing with the Registrar of Joint Stock Companies a statement in lieu of prospectus, together with a statutory declaration such as a public company is required to file before commencing business. The privileges of private limited companies are more numerous than those set out above, and amongst the more important are—

(a) Power to be incorporated with a minimum of two members instead of seven;

(b) Exemption from the requirements as to filing a statutory report prior to the statutory meeting;

(c) Exemption from the necessity of filing a prospectus or statement in lieu of prospectus (*q.v.*);

(d) Exemption from restrictions as to commencing business and restrictions as to minimum subscriptions.

Quite apart from statutory privileges, the advantages of limited liability are so manifold, that private companies are likely to be much more numerous than are limited partnerships, one great advantage being that they are subject to statutory audit, although at present no standard of qualification is laid down for the auditor of a joint stock company.

PROBATE.

(See EXECUTORS AND ADMINISTRATORS; WILLS.)

PROCESS COSTS.

(See COST ACCOUNTS, p. 346.)

PRODUCTIVE EXPENDITURE.

(See REVENUE EXPENDITURE.)

PROFIT.

The increase of capital consequent upon the employment of the original capital in manufacturing, trading, or conducting a public undertaking. (See also ACCUMULATED PROFITS; AUDITING, p. 84; PROFIT, ANTICIPATION OF.)

PROFIT AND LOSS ACCOUNT.

A Profit and Loss Account is a statement designed to show the amount of net profit earned by a commercial or financial business, by a professional firm or by an individual, or the amount of the actual loss sustained during the period embraced by the account. It also shows, in the case of a private individual, or any concern whose income is derived solely from property or investments, what is the ultimate net revenue from the property or investments after the income derived therefrom has been charged with the expenses of administration. As a rule, the term "Revenue Account" is usually applied to this latter statement, as explained hereafter.

When a Profit and Loss Account is prepared from a set of books kept on the system of double entry, it is prepared from the Trial Balance by an extraction of those entries on the debit and credit side which have not been already extracted in the preparation of a Trading Account, or which have to be left to be taken out in connection with the preparation of the Balance Sheet, as explained in the article dealing with that statement.

Before proceeding with an explanation of the various items which are usually included in Profit and Loss Accounts, it will be as well to point out the difference between three forms of accounts which are very often confused with each other, but which have different characteristics, namely: a Receipts and Payments Account; an Income and Expenditure or Revenue Account, and a Profit and Loss Account.

RECEIPTS AND PAYMENTS ACCOUNT.—A Receipts and Payments Account is a statement which contains on the debit or left-hand side the actual amount of cash received during the period, quite irrespective of the fact whether it is received in respect of transactions which occurred during the period, or whether the receipts are in respect of goods delivered or for services rendered prior to that date, or receipts in advance for transactions to be carried out after the date of the account; while on the credit or payments side will be included the cash actually expended during that period. In both cases the items are usually grouped under appropriate headings.

In other words, where the books of an individual or concern have been properly kept, this account is an abstract of the total receipts and payments as shown in the Cash Book, including usually the balances at the commencement and at the end of the period.

INCOME AND EXPENDITURE ACCOUNT.—

An Income and Expenditure Account, a Revenue Account, and Profit and Loss Account shows on the credit side the total income which appertains to that period, or the earnings of the period, quite irrespective as to whether they have been received during that period or not; subject, however, as explained hereafter, to any allowance that may be made in respect of income which ought to be received but which, for some reason or other, is expected may never be collected.

On the debit side of this account will be charged all the expenditure incurred during that period, whether payment thereof has been made or not, and therefore all liabilities of the concern incurred up to the date on which the account is closed and which will be brought into the Balance Sheet as liabilities will be included.

It may here be stated that the term "Income" is now usually employed by professional accountants to denote the actual or estimated revenue for the period, as opposed to the word "Receipts," which is now only applied to the actual money received during that period.

The term "Expenditure" includes all items of expense incurred during the period, as opposed to the word "Payments," which is solely applied to the amounts actually paid. As a consequence, such wording as is frequently seen at the heading of accounts, as "Receipts and Expenditure," or "Income and Payments" is incorrect, they not being co-relative terms.

REVENUE ACCOUNT.—The term "Revenue Account" is usually used in connection with the statements prepared for private individuals and concerns whose income is not derived from trading, such as those showing the financial result of the transactions of landlords, trust and finance companies, land companies, etc., while the term "Profit and Loss Account" is usually made use of by commercial undertakings, who frequently combine in that account the Trading Account instead of dividing it into two statements as is recommended and as is the general practice.

TRADING ACCOUNT.—When the Trading Account of a concern is combined with the Profit and Loss Account, the compilation of the account is prepared on practically the same lines, except that the items brought into the account include those which will be found described in the article on the "Trading Account," in combination with those referred to in this article.

EXAMPLES OF PROFIT AND LOSS ACCOUNTS.

—Before proceeding with remarks on the items

which usually appear in Profit and Loss Accounts, a few examples of this statement are given on pages 785 and 786, which should be studied, so that the form may become familiar to the student.

The Profit and Loss Accounts of many companies, as submitted to the shareholders, do not show clearly on the face of the account the actual net profit of the concern; in other words, it does not show the financial result of the transactions of the concern for the period embraced by the account. For example, such accounts frequently commence with a balance brought forward from the Profit and Loss Account for the preceding period, include particulars of interim dividends paid to shareholders, and conclude with a balance which, as a result of these entries being included, is not the balance showing how much profit or how much loss has resulted from the transactions of the period.

To show the actual profit for the period it is necessary that the account should not contain any entries relating to past or future transactions. In other words, no entries which do not relate to the period in question should be included.

DIVISION OF PROFIT AND LOSS ACCOUNT.

—It is, therefore, most desirable that the Profit and Loss Account of a company should be divided into two parts: the first part being the real Profit and Loss Account for the period, the construction of which it is the object of this article to explain, resulting in a balance which would be the net profit or actual loss for the period. This balance should be carried down into the suggested second part or division, to which should also be carried the balance, if any, brought forward from the previous account, the amount of any interim dividend or dividends, if any paid, resulting in a balance which should be carried into the Balance Sheet, thus closing the account.

METHOD OF PREPARATION.—The actual method of preparing the Profit and Loss Account from the Trial Balance, in the case of books kept by a system of double entry or by other means when the books of account are kept on the single entry system, or when no books are kept at all, but only memorandums of transactions are treated in works on book-keeping. The object of this article is to guide the compiler of the Profit and Loss Account to decide on the actual amounts to be included in the statement, under the various headings, among which the income or expenditure shown on the statement is to be divided.

CREDIT SIDE.—As a rule, the Income or Revenue is shown in the Profit and Loss Account on the right-hand or credit side, while the expenditure is stated on the left-hand or debit side. This is the proper method of preparing such a statement, but for some reason or other difficult to understand in the Revenue Account of an

THE INTERNATIONAL INSURANCE COMPANY

REVENUE ACCOUNT.—FOR THE YEAR ENDING 31ST DECEMBER, 19..

(Pursuant to the Assurance Companies Act, 1909, First Schedule.)

Dr.				Cr.
	£		£	£
Amount of Life Assurance Fund on the 1st		Claims under Policies Paid and		
January, 19..	1,000,000	Outstanding—		
Premiums	150,000	By Death	60,000	
Consideration for Annuities Granted	20,000	„ Maturity	15,000	
Interest, Dividends, and Rents—				75,000
Less Income Tax thereon	29,900	Surrenders, including Surrenders of		
Assignment Fees, etc.	100	Bonus		20,000
		Annuities		45,000
		Commission		18,000
		Expenses of Management		15,000
		Bonuses in Reduction of Premiums		5,000
		Investment Reserve Fund		10,000
		Amount of Life Assurance Fund on		
		the 31st December, 19.., as per		
		Third Schedule		1,012,000
	<u>£1,200,000</u>			<u>£1,200,000</u>

THE FOREIGN TRADING CO., LTD.

PROFIT AND LOSS ACCOUNT.—FOR THE YEAR ENDING 31ST DECEMBER, 19..

Dr.			Cr.
	£		£
To Directors' Fees	600	By Gross Profit from Trading Account	1,790
„ Office Rent and Salaries	250	„ Transfer Fees, etc.	10
„ General Expenses	360	„ Commission, London	200
„ Cablegrams	25		
„ Postage and Telegrams	35		
„ Printing and Stationery	125		
„ Audit Fee	105		
„ Balance, being profit transferred to Balance			
Sheet	500		
	<u>£2,000</u>		<u>£2,000</u>

MESSRS. A B & CO.

PROFIT AND LOSS ACCOUNT.—FOR YEAR ENDING 31ST DECEMBER, 19..

Dr.			Cr.
	£		£
To Rent	400	By Balance brought from Trading Account	8,800
„ Salaries	1,100	„ Interest on Partners' Drawings	200
„ Wages (Messengers and Boys)	180		
„ Rates and Taxes	350		
„ Interest on Capital	170		
„ Balance, being net profit subject to Income			
Tax charged against Partners' Capital			
Accounts	6,800		
	<u>£9,000</u>		<u>£9,000</u>

THE UNIVERSAL BREWERY CO., LTD.

Dr. PROFIT AND LOSS ACCOUNT.—1ST JANUARY TO 31ST DECEMBER, 19..

Cr.

	£		£	£
To Salaries, Wages, Cost of Delivery and Carriage, Horse and Stable Expenses, Travelling Charges and Agency Expenses, etc.	15,000	By Gross Profit brought from Manufacturing and Trading Accounts		50,800
„ Trade Discount and Allowances to Customers	5,000	„ Rents received and accrued on Public Houses and other Properties	6,000	
„ Repairs to Houses, etc.	4,000	Less Rents paid on Leaseholds and Abatements and Quit Rents, etc.	2,000	
„ Depreciation on Brewery Buildings	1,500			4,000
„ Depreciation—		„ Balance of Interest Account		200
On Leaseholds, etc.	£1,600			
„ Various Assets	2,000			
	3,600			
„ Trustees' Fees	200			
„ Directors' Fees	1,200			
„ Bad Debts written off	500			
„ Compensation Fund Charge	600			
„ Interest on First Mortgage Debentures, less Tax	7,500			
„ Balance carried to Balance Sheet being Net Profit.	15,900			
	<u>£55,000</u>			<u>£55,000</u>

THE INDUSTRIAL CO-OPERATIVE SOCIETY, LTD.

Dr. PROFIT AND LOSS ACCOUNT.—1ST JANUARY TO 31ST DECEMBER, 19..

Cr.

	£	£		£
To Salaries and Wages of Staff, and contributions under the National Insurance Acts		65,000	By Balance from Trading Account	116,100
„ Sundry Rents		4,000	„ Rents	400
„ Lighting, Rates, Insurance, Income and other Taxes		6,000	„ Advertisements in Price Lists	1,500
„ Stationery and Printing		2,500	„ Interest on Investments	2,000
„ Price Lists and Circulars		1,200		
„ Postage		1,600		
„ Trade and Miscellaneous Expenses		6,000		
„ Legal Expenses		200		
„ Remuneration of Chairman and Directors		1,500		
„ Maintenance and Repair of Buildings, etc.		3,100		
„ Depreciation of Fixtures and Furniture		1,200		
„ Interest—				
On Deposit Accounts	1,100			
„ Debentures	4,000			
		5,100		
„ Donations and Subscriptions		400		
„ Written off King St. Premises		600		
„ „ Dover Premises		400		
„ Balance, being profit carried to General Balance Sheet		21,200		
		<u>£120,000</u>		<u>£120,000</u>

assurance company, the form for which is prescribed by the Assurance Companies Act, 1909, the Income is placed on the left-hand or debit side and the Expenditure on the right-hand or credit side. (See p. 785.)

TRADING ACCOUNT: BALANCE BROUGHT THEREFROM.—The income side of the Profit and Loss Account of a trading concern usually begins with the balance brought from the Trading Account, which balance is usually described as the "gross profit." This item requires no comment here as it is the actual balance found as the result of the method in which entries have been made on the debit and credit side of the Trading Account, and the method of arriving at that balance will be found in the article dealing with the preparation of the Trading Account. For the purpose, therefore, of the Profit and Loss Account its accuracy must be assumed.

INTEREST ON INVESTMENTS.—The amount taken to credit in respect of interest or dividends on the investments held by the concern should be the interest which has accrued during the period embraced by the account. In the case of interest on Government securities, debentures of railway and other commercial companies it is easy to calculate the amount applicable to the period. When the concern holds ordinary or preference shares in companies the necessary calculation cannot be made, as unless the statement is prepared at some considerable date after the termination of the period the dividends which will be declared by the companies, whose shares the concern holds, cannot be calculated. It is therefore the ordinary practice to take credit only for dividends on the shares of companies which have been actually paid and received by the concern during the period embraced by its Profit and Loss Account, or at the most to take credit for dividends which have been announced, although not actually paid, during that period. Under no circumstances should the concern take credit for any interest or dividend which accrues to the period after the date to which the Profit and Loss Account is made up.

INTEREST ON MORTGAGES.—In this case, where it is considered desirable to show the interest received on moneys lent on mortgage, the compiler of the Profit and Loss Account should include under this heading the actual interest appertaining to the period embraced by the account.

As a rule, a register of the amounts lent on mortgage is kept, and the compiler of the statement should ascertain from the register the amount of each mortgage and the rate of interest it carries, so as to ensure that the amount taken credit for will be correct.

INTEREST ON LOANS.—This item occurs in the Profit and Loss Accounts of banking and other

financial concerns, and whether or not it appears as a separate item on the face of the account it necessitates the same care. The interest taken credit for should be only the amount which it is confidently expected will ultimately be received, and the compiler of the statement should ascertain whether the interest taken credit for in the previous Profit and Loss Account has been received or is still outstanding. Should the latter be the case, he should make careful inquiry of the person best fitted to give him the necessary knowledge, and if there is any question as to its ultimate payment it is prudent to reserve either the whole of the interest or a certain proportion of it. It would also be as well that he should inquire as to whether the principal itself is likely to be recovered, as if there is any doubt as to the principal there can be very little doubt that the interest on this principal should not be taken credit for without a proper reserve being made. The interest should include the accrued interest to the date of making up the account, the balance unpaid being brought into the credit side of the Balance Sheet amongst the debtors.

PREMIUMS.—This item is, as a rule, the principal one on the credit side of an insurance company, whether life, fire, accident, burglary, etc. In the majority of insurance companies these premiums are collected by means of agents, and the compiler of the Profit and Loss Account should be careful to include only such amounts as it is reasonably expected will be recovered. The total amount of the premiums appertaining to the period embraced by the account should be taken credit for after an allowance has been made for any possible loss on their realisation, but no deduction should be made for the commission payable to the agents or for other expenses, whether for rent, salaries, etc., as these items should be inserted amongst the expenditure.

It is the practice of some insurance companies, especially fire, to accept from an insurer six years' premiums in one payment, and to treat this as in full payment of premiums for seven years. In such cases the six-year premiums should be treated as being a premium for seven years by dividing the premium into seven equal amounts, and make a proportionate reserve, usually by deduction from the amount taken credit for.

CONSIDERATION FOR ANNUITIES GRANTED.—It is the practice of most life assurance companies to grant annuities to persons on receiving from them a fixed payment. The total amount received during the period embraced by the Profit and Loss Account should be taken credit for on the Income side, and the amount to be reserved or either deducted or charged on the other side of the account, being a matter for actuarial calculation, the compiler of the statement should confer with the actuary when settling the amount to be

taken credit for and obtain from him the result of his calculations.

TRAFFIC RECEIPTS.—This item appears in the accounts of railway, tramway and omnibus companies. In the case of railways, this is arrived at by a somewhat complicated system of accounts which pass through the railway audit office, and the compiler of the statement must satisfy himself that full allowance has been made for all returned railway tickets which may be admitted by the company, and also that the necessary deduction has been made in respect of any portion of season tickets unexpired.

The traffic receipts of tramways and omnibus companies are more readily ascertained. They are collected as a rule on the journeys by collectors or conductors, and their returns are periodically checked by inspectors. With a few exceptions there are no return of tickets to be allowed for and no season tickets.

SHARES IN COMPANIES.—The credit side of the Revenue Account of trust and other financial companies frequently includes amounts taken credit for in respect of shares in companies which have either been promoted by the trust or finance company, or for which it has underwritten an issue of capital, receiving as part or full remuneration an issue of fully paid shares.

The compiler of the Revenue Account should exercise great care in arriving at the amount to be taken credit for in the Revenue Account in respect of these shares, as should too large a sum be included and a dividend paid to the shareholders in cash on the strength of this amount being in excess of what should be taken credit for, the directors of the concern, and possibly even the compiler of the account, might be subject to an action at law in the event of the trust or finance company going into liquidation.

The best plan for the compiler of the Profit and Loss Account to adopt is to prepare in the first place a special statement, placing on the credit side, in separate columns, the amount received in connection with the underwriting in cash and the value of the shares so acquired, treating the shares at the price issued to the trust or finance company, and a third column, the cash received, if any, on the realisation of some of these shares. On the other side place the amount expended by the trust company in connection with the underwriting, or the cost of promotion, if the company has been promoted by the trust company, and if any of the shares received in connection with the promotion or underwriting have been paid away to other persons this should be placed in a separate column. A balance should then be struck between the cash received and paid columns, and the amount of the shares received and disposed of columns, and credit should only be taken in the Profit and Loss

Account or Revenue Account for the amount actually realised in cash. In future statements credit can be taken for the net realisation of these shares.

PREMIUMS ON ISSUES OF SHARES.—When a company in a flourishing condition wishes to raise fresh capital it is very often the custom to offer its shares at a premium, the premium being at a slightly lower rate than that prevailing on the Stock Exchange at the date of issue. As these shares can only be inserted at their par value on the debit side of the Balance Sheet, the premium is practically a profit, and the directors are entitled legally to bring this profit to the credit of the Profit and Loss Account, and even make use of it in connection with the payment of a dividend. The most prudent course, however, to adopt in connection with this profit is first of all to pay all the expenses in connection with the issue out of it and place any surplus there may be to the credit of a permanent reserve.

TRANSFER FEES.—It is the practice for every company to require a small fee (in the case of limited liability companies usually fixed by the Articles of Association) for registering transfers of shares sold to other proprietors or a new proprietor called the transferee. In the case of those companies where there is a considerable amount of dealing on the Stock Exchange in the shares the fees come to an appreciable amount, in which case they usually appear as a separate item on the credit side of the Profit and Loss Account. If the fees are very trifling in amount, there is no objection to them being included in some general item of Revenue, such as Sundry Revenue.

EXCHANGE.—In companies transacting business abroad, a profit in connection with the difference of exchange between this country and the countries with whom the business is transacted is sometimes considerable, in which case it is as well that this profit should be shown clearly on the face of the Profit and Loss Account under a separate heading. The compiler of the Profit and Loss Account should only insert the actual amount which it is clearly expected will be realised at the close of the open transactions or else confine it to the amount actually realised.

RENTS.—In the case of owners of property, whether agricultural or town or both, and also in the case of companies whose business it is to own and manage property whether their particular item of revenue is derived from rents or not, the amount taken credit for may include not only rents due up to the last quarter day but rents in arrear, if it is fully expected that such rental will be received. In order to guard against the omission of rentals the compiler of the Profit and Loss Account should examine the Rent Roll, either with what is sometimes called a "Terrier," or a register of rents, whether farm, house, cottage or

allotments, so as to be able to include all rents applicable to the period. Where no rental is brought to credit in respect of any holding he should make inquiries from the surveyor, or whatever the name of the agent may be who attends to this business, and learn the reason for the omission. If the Profit and Loss Account is made up to a date not coinciding with the quarter day, the rentals should strictly be apportioned, and credit may be taken for the accrued rental up to the date of the Profit and Loss Account, but many landlords, in order to be on the safe side, will only take credit for the rent accrued to the previous quarter day.

DEBIT SIDE.—Dealing now with the items which are most usually found on the debit or expenditure side of the Profit and Loss Account, it may first be stated generally that this side of the statement should include all items of expenditure of the concern applicable to the period which have not already been charged against the Trading Account and, in addition, those items which come under the description of "depreciation" and "reserves."

It will be convenient first to deal with two items which are practically a first charge not only on the income but also on the capital of the concern. The second item refers exclusively to the capital of a company.

INTEREST ON MORTGAGES.—Under this heading should be included the interest payable by the concern on all moneys which have been borrowed by the concern in respect of which it has executed mortgages on either freehold or leasehold property. If the books of the concern have been properly written up the balance in the Ledger Account under this heading should include the interest accrued up to the date to which the Profit and Loss Account is prepared. In any case, the constructor of the account should satisfy himself that this is the case, and that the full interest applicable to the period is charged. It would be as well if he could ascertain from a perusal of the mortgage deed that the rate of interest on which the calculations have been made is the rate stipulated for in the deed. In many mortgage deeds it will be found that the rate of interest may vary; in other words, it may be raised after a certain number of years have elapsed or reduced after a fixed period. In many cases, the rate of interest is stated, with a clause inserted in the deed to the effect that on certain conditions, such as prompt payment, the actual interest to be paid is of a slightly lower amount, and these matters have to be borne in mind in the preparation of the Profit and Loss Account.

INTEREST ON DEBENTURES.—The debentures of a company are sometimes secured by a specific mortgage on some or all of the freehold or

leasehold property of the company, in which case the same plan should be adopted as already referred to, namely, an inspection of the mortgage deed, and the interest calculated in accordance with the terms found therein. The majority of debentures, as a rule, are issued having merely a general charge on the assets of the company, but, in either case, the preceding remarks as to accrued interest applies in the case of interest payable to those who have advanced money to the company on debentures secured by a floating charge. Where there has been more than one issue of debentures the constructor of the Profit and Loss Account should ascertain the terms on which each class of debenture has been issued, the amount issued for each class, the rate of interest, and the date of payment in each case, so that the full amount of interest accrued due at the closing date of the Profit and Loss Account may be charged.

INTEREST ON LOANS.—The same care must be taken by the compiler of the statement in connection with the amount to be charged in respect of interest on any moneys which have been borrowed without security, both as to the amount of each loan, and the rate of interest each loan bears.

INTEREST ON CALLS PAID IN ADVANCE.—The Articles of Association of companies registered under or operating under the Companies (Consolidation) Act, 1908, usually authorise the payment by members of their calls in advance of the date fixed by the directors for the payment of such calls, interest thereon usually mentioned in the prospectus being allowed. As these payments will be for various sums and on various dates, a special calculation will have to be made in respect of the interest payable on every call paid in advance, and the constructor of the Profit and Loss Account should therefore check a specially prepared schedule showing the amount of the calls, the date on which they were respectively due, and the date on which they were respectively received; or, should the constructor be the book-keeper himself he should, for his own protection, make the requisite schedule before making the entries in the books, and have it checked by an independent person. He should also see that the full interest is calculated up to the date of the account.

CLAIMS UNDER POLICIES PAID AND OUTSTANDING.—The principal charge against the Revenue Account of insurance companies of every description, whether life, fire, marine, guarantee, accident, burglary, etc., are the claims which are made under its policies, and for the purposes of the Profit and Loss Account such claims may be divided under three heads—

(1) Claims which have arisen during the period and settled during the period.

(2) Claims which have arisen during the period and have been agreed but not paid.

(3) Claims which have been made, but which have not been adjudicated upon and consequently have not been paid.

There may also be added a fourth item which affects the amount, namely, as to whether any estimate in respect of claims made before the close of the preceding Profit and Loss Account and charged in that account has been exceeded in amount on settling such claims, or whether the estimated amount charged was in excess of what ultimately had to be paid. In the first case, the amount to be inserted opposite the item "Claims under Policies," would be augmented, while, in the latter case, the amount would be diminished.

By the Assurance Companies Act, 1909, the Revenue Account of every assurance company, in respect of its life assurance business, is required to divide both its income and expenditure into three columns: one showing the amount applicable to its business within the United Kingdom; the second, to its business out of the United Kingdom; and the third column has to contain the totals of the first and second columns. This division does not apply to fire, marine, accident, or other insurance business.

ANNUITIES.—This item appears in the accounts of practically all life assurance companies and, strictly speaking, should include the accrued amount in respect of all annuities up to the date on which the Revenue Account is closed. The compiler of the Revenue Account should be careful to include the proper amount in respect of all annuities which have come into force during the period of the account, and he should also be careful to exclude any charge in respect of annuities which may have lapsed, owing either to the death of the annuitant, or the arrival of the periods on which date annuities for a fixed term also lapse.

COMMISSION.—It is the practice in businesses of many descriptions for certain employees to be remunerated by commission, either on the gross amount or on the net amount, after deducting therefrom certain expenditure, or by a commission on the profits. In every case the compiler of the Revenue Account must exercise the greatest care in arriving at the amount to be charged.

In many life assurance companies a considerable part of their business is introduced through agents appointed in various towns in the United Kingdom, or in the Dominions or abroad. It is also the practice of many commercial houses to employ travellers who are paid a commission on the value of the orders they transmit to their employers. In many cases travellers of this description and other agents are paid a fixed sum by way of salary and a commission in addition, and in these cases there must be a distinct separation in the Revenue or Profit and Loss Account as the case may be, so that the actual amount paid in commission only

is included under this heading. A great point the compiler of the Revenue Account has to bear in mind is that the commission chargeable in the account must be the commission actually appertaining to the amount taken credit for on the other side of the account on which the commission is payable, with the result that agents and travellers payable by commission will, as a rule, appear on the debit side of the Balance Sheet for commission earned by them on business done, but perhaps not payable to them until the money has been received by the employers in respect of such business.

EXPENSES OF MANAGEMENT.—The method of setting out in a Profit and Loss Account the various expenses connected with the carrying on of the concern whose accounts are being prepared varies according to the nature of the business. In some concerns the whole of them are grouped together under one general heading, such as indicated above; in others, they are set out in very full detail, and no directions can possibly be given, but the grouping of the various items must be left to the compiler of the statement, subject to any instructions he may receive from his superiors, such as a board of directors, or the partners of a firm. Items which usually come under this heading are dealt with separately, but it must be distinctly understood that if two or more of these items are grouped together, the heading under which they are grouped should not in any way be misleading.

RENT.—There should, naturally, be included under this heading the actual rent payable in respect of all the premises occupied by the concern for business purposes, and if the account is being prepared to a date not coinciding with any of the recognised quarter days, the accrued rent to the date of making up the account from the previous quarter day should be calculated and included in the amount. Unpaid amounts would naturally appear amongst the creditors, although the accrued amount would not actually be due at that date. Should some of the premises not be fully required for business purposes, and be let off to other tenants, the question has to be decided as to whether the total amount payable should be charged against the Profit and Loss Account and the amount receivable brought to credit, or whether the amount receivable should be deducted from the amount payable, and only the balance charged against the Profit and Loss Account. It would be difficult to state that either way would be incorrect.

RATES.—When inserting the amount in respect of this item, the compiler of the statement will seldom have to ensure that the full amount is inserted, as rates are usually collected in advance, and in this case should the owner of the business or the directors of a company wish it, the proportion of the amount paid which appertains to the

period between the date of the statement and the date up to which the rate has been paid may be deducted, which would have the effect of bringing that amount into the credit side of the Balance Sheet as an asset. This is undoubtedly the strictly professional method of fixing the amount chargeable, but many owners and directors prefer the amount paid to be the amount charged in the statement, which practically leaves the balance as a secret reserve.

TAXES.—The amount to be inserted in respect of this item should, as in all other cases, be the amount appertaining to the period, and the compiler must therefore carefully peruse the demand notes and arrive at the proper amount. He should also be careful to ascertain that if any of these taxes have to be paid by an outsider, such as the ground landlord or tenants in respect of any of the properties for which the concern has first of all to pay the tax, that the proper persons are treated as debtors for the amount. There is no objection to including the Income Tax on profits or any Government tax such as the temporary Excess Profits Duty and Corporation Profits Tax, but as Income Tax, Excess Profits Duty, and Corporation Profits Tax are only payable on profits it is better that these amounts should be inserted in what has been referred to as the Supplementary Statement or Appropriation Account.

REPAIRS AND RENEWALS.—This is an item which may be dealt with in various ways.

(1) By adding all amounts expended to the Capital Account or the credit side of the Balance Sheet, and charging against the Profit and Loss Account an amount which is frequently a percentage of the Capital Account thus increased.

(2) By charging the entire amount against the Profit and Loss Account.

(3) By placing the whole amount to a Suspense Account and charging the Profit and Loss Account with the amount which may be deemed applicable to the period, having regard to the fact that some of the repairs may very properly be chargeable against one or more of the following years.

(4) By raising a Suspense Account and charging the Profit and Loss Account with what is considered the annual average outlay in respect of repairs and renewals even before any expenditure has been incurred.

It is difficult to state as a general rule which of these four operations should be selected, as so much depends upon the extent and state of the buildings, the plant and machinery, or whatever property of the concern has to be kept in efficient order by means of repairs and renewals. The main object of the compiler of the statement should be to charge fully the statement in respect of this class of expenditure, so that there is not left on

the credit side of the Balance Sheet expenditure which is not at the date of the Balance Sheet fully represented by value, having regard to it being the expenditure of a going concern.

DIRECTORS' FEES.—The amount to be inserted on the debit side of the Profit and Loss Account in respect of these fees may consist either of a fixed amount only or a fixed amount as minimum fees, supplemented by commission either on the profits or on the dividend paid to shareholders. In any case, the compiler of the account should ascertain the amount that is absolutely legally due to the directors in respect of the period embraced by the account. The Articles of Association of all limited companies, or, as the case may be, Table A, if there are no special Articles of Association, should be consulted as the remuneration of directors is either a fixed amount, settled by those articles, or there may be found a clause therein directing how the directors' remuneration is to be calculated. If the directors claim any higher fee than that stated in the Articles of Association, on the ground that the shareholders have increased it, the compiler of the account should satisfy himself first of all that the shareholders are empowered by the Articles to vote an extra sum, and the minutes of the meeting at which the sum was voted should be inspected by the compiler. In the case of a percentage or commission, either on the turnover or the profits, the compiler should be very careful in calculating the amount, and before inserting it in the Profit and Loss Account should agree the amount with the directors.

SALARIES.—In the accounts of small concerns, salaries and wages are frequently placed under one heading, but in the accounts of concerns which employ several or a number of clerks in the office, and a number of working men in the factory, mine, or whatever the concern may possess, it is usual to separate them, and as referred to in the Trading Account, a large proportion of wages is charged in that account. Whether, however, salaries and wages are placed under one or two headings, the remarks fully apply.

The term "salaries" is usually applied to the senior employees, such as the secretary and manager, also to all clerks in the office, including messengers, etc., as apart from those performing manual work. The amount of the fixed salaries to be inserted in the Profit and Loss Account presents no difficulty. When, however, any members of the staff receiving a salary are paid in addition a commission, either on any particular department or on the total amount of the business done by the concern or on the gross or net profit of the concern, and it is desired that this should not be placed under the heading of Commission but be included amongst the salaries, the compiler of the statement should read the preceding

remarks, which specially relate to commission of this nature.

In the case of a company, the fees of the directors should not be included in "Salaries," but should be stated either by itself, or if included under the same heading as salaries, it is usual to describe the item as "Directors' Fees, Salaries, etc."

WAGES.—All amounts expended in wages, which have not already been charged against the Trading Account, must be included amongst expenditure in the Profit and Loss Account. As wages are usually paid weekly the amounts to be inserted in the statement present no difficulty, and the only comment necessary is that, if any special bonus is given to the wage-earning members of the staff, the compiler of the Profit and Loss Account should take steps to ascertain the full amount of such bonus as appertains to the work taken credit for on the other side of the statement should be included.

TRADE DISCOUNT.—In many concerns goods are invoiced to the purchasers at prices which are subject to a deduction on payment. The compiler of the Profit and Loss Account should ascertain the amount of discount of this nature which may be claimed by the various debtors of the concern, and if the amount is included in the Balance Sheet under the item of "Sundry Debtors," the full amount should be charged against the Profit and Loss Account under the above heading, but the better plan is for this to be deducted from the total sales, in which case the item need not appear on the expenditure side of the Profit and Loss Account.

CHARITABLE DONATIONS.—Many concerns frequently do business in foreign countries and make voluntary donations for charitable purposes, for example, many merchants, bankers, etc., if they hear of an earthquake or a flood having taken place in some part of the world where they transact considerable business, send very large amounts to the fund being raised for the relief of the sufferers. Many mining and manufacturing concerns make annual contributions and occasional donations to hospitals and infirmaries in their district. These amounts should, as a rule, especially in the case of companies, be clearly set out in the Profit and Loss Account of the concern, but, unfortunately at the present moment, although it is a distinctly legitimate charge against the profits of the concern, as it is clearly not the object of a business firm or company to make contributions of this sort except from a purely business point of view, it is not allowed to be deducted when computing the amount on which Income Tax and other Government taxes are payable, unless a concrete benefit is conferred on the business by the donation, *e.g.* hospital services to employees.

It is impossible to deal with other items which

might occur in a Profit and Loss Account having regard to the multifarious businesses which are transacted. The items already referred to are quite sufficient to indicate to the compiler of any Profit and Loss Account the principle on which any item not dealt with has to be treated.

There now remains for consideration a few items which frequently have to be charged against the Profit and Loss Account, although no actual expenditure may have occurred, and, consequently, there will not be a balance of a Ledger Account found in the Trial Balance to call attention to it. There are also a few items which may be found in the Trial Balance and which require special treatment.

DEPRECIATION OF WASTING ASSETS.—

The compiler of the Profit and Loss Account has to consider very carefully the amount which he must charge in his statement in respect of wear and tear, and obsolescence of perishable assets and for the gradual decrease in value of assets, such as buildings on leasehold property, plant, machinery, workmen's tools, etc.

This subject is very fully dealt with in the article **DEPRECIATION**, and it is consequently not necessary to go into any details in connection therewith. The arriving at the proper amount to be charged by the compiler of the Statement in respect of each "wasting asset" is a very important part of his responsible duties.

ALLOWANCE FOR BAD DEBTS.—It is seldom that a business of any kind, and certainly not one of any magnitude, which can be carried on without a loss occasionally occurring on the realisation of the item known as "Sundry Debtors." It is quite impossible, however careful those who conduct a business may be where credit is given, not to make an occasional loss when trying to realise the debts shown on the books. It is seldom, therefore, safe to count that the total amount due from the debtors will be realised without making an allowance for a possible loss and also providing for a loss on debts when it has absolutely been ascertained they will not be paid in full. The compiler of the Profit and Loss Account should, therefore, go carefully through the list of debtors and make inquiries from the heads of the departments where these debts have been incurred and discuss with them the probability of their being paid in full or being partially paid, or if the financial position of the debtors is such that the concern may not ultimately receive anything. Having compiled a list the total estimated loss which will accrue should then be charged against the Profit and Loss Account.

RESERVE AGAINST DEPRECIATION OF SECURITIES.—The compiler of the Profit and Loss Account should ask to be provided with a list of the securities at the price at which they appear in the ledgers. He should then ascertain the

market price of these securities, and if the total of the market price is below that of the total book value he should charge the Profit and Loss Account, under the above or a similar heading, with a sum at least equal to this amount. Some employers may think it desirable to increase this amount, more especially if they think there is going to be a further decline in the market price.

LOSS ON REALISED SECURITIES.—Should any of the securities have been realised since the date of the previous statement of accounts the amount will be an ascertained fact, and there will therefore be no difficulty in knowing what is the proper amount to be charged against the Profit and Loss Account.

PRELIMINARY EXPENSES: AMOUNT WRITTEN OFF.—The expenses in connection with the formation of a company, such as the obtaining of an Act of Parliament or the cost of the registration of a company under the Companies (Consolidation) Act, 1908, including the law costs, the preparation of all legal documents transferring property or other assets to the company, the cost of advertising the prospectus, brokerage, commission (if any) paid, etc., are usually brought together into one Ledger Account styled "Preliminary Expenses."

As it would be unfair to charge the whole of these expenses against the first year's working of the company, it is usual to spread this expenditure over a certain number of years, which should not, as a rule, exceed five, and charge an equal amount of this expenditure for each of these years until the amount is finally written off, any balance which may remain being carried to the credit side of the Balance Sheet. The number of years decided over which to spread this expenditure, and the consequent amount to be charged each year, should be settled by the directors before they have ascertained the profits for the period, as it is most unwise that they should be influenced in deciding upon the number of years over which to spread this expenditure by the effect it may have upon the dividends to be paid to the shareholders. This expenditure is really as much a charge against the profits of a company as any of the actual working expenses for the period embraced by the account, though, unfortunately, there is a tendency to consider that the amount to be charged against any year's Profit and Loss Account has to be dependent upon the profits of the period.

MISCELLANEOUS ITEMS.—It is quite impossible to discuss in detail every item which might possibly occur, either on the income or expenditure side of a Profit and Loss Account, but the items which have been dealt with in detail will be a sufficient guide in considering how to deal with those items which have not been treated.

When the items of the Trial Balance which have

to be dealt with in the Profit and Loss Account have been finally brought into the Profit and Loss Account, there naturally results a balance either of profit or of loss. Should the total of the credit side exceed that of the debit, the result is naturally a profit, provided, of course, each item has been properly dealt with, and this amount should appear as the balancing item on the debit side of the statement. On the other hand, should the total of the debit side be the higher of the two, the financial result of the transactions is a loss and the amount should appear as the balancing item on the credit side of the statement. The profit or the loss, as the case may be, is then either carried into the Balance Sheet or taken to the second part of the statement already referred to, usually called an "Appropriation Account."

Before, however, referring to this statement, it may be as well to explain that the Profit and Loss Account referred to in this article is that form of account which prevails in nearly all trading concerns, and the concerns of all commercial or professional men, but there are practically four systems of accounts known both to lawyers and accountants for ascertaining the profits of companies. To those who wish to study them the writer can only refer them to Chapter XIV of the eleventh edition of his work, "Auditors, Their Duties and Responsibilities."

APPROPRIATION ACCOUNT.—The Appropriation Account, which may be either set out as a separate statement or placed at the foot of the Profit and Loss Account as a continuance or what is practically a completion of that statement, is formed by transferring to it the balance of the Profit and Loss Account and also bringing into it, on its proper side, the balance of the previous Profit and Loss Account, the Income Tax chargeable on such profits, which must necessarily be a matter of calculation, the Corporation Profits Tax, the Excess Profits Duty, and any interim dividend paid since the date of the previous accounts.

If the Profit and Loss Account has resulted in a loss then these items will naturally increase the adverse balance to be carried into the Balance Sheet; if it show a profit, these items will naturally diminish the amount of profit to be brought into the Balance Sheet, or they may convert the profit shown on the Profit and Loss Account into a real loss from the shareholders' point of view.

The reason for having an Appropriation Account or dividing the Profit and Loss Account into two portions is that Income Tax, Corporation Profits Tax, Excess Profits Duty and dividends, whether interim or final, are not a charge against profits from the taxable point of view, but an appropriation of profits, although Income Tax is not payable on the profit diminished by other taxes

collected by the Crown. (See also ACCOUNTS, CRITICISM OF, pp. 12, 15; INVESTIGATIONS, p. 574.)

PROFIT, ANTICIPATION OF.

(a) The allocation of profits, as, for example, by way of dividends, which have not yet been earned, in the expectation that such profits will be earned during the remainder of the company's financial period.

(b) The making of profit by valuation of assets, especially stock, at an appreciated value, in the anticipation that such value will be maintained and the profit realised.

PROFITS, ADJUSTMENT OF.

(See INVESTIGATIONS, p. 577.)

PROFITS, AND PROFITS AVAILABLE FOR DIVIDEND.

The subject is one of extreme difficulty in practical application, though readily comprehensible in theory, and full of generalities and matter for diversity of opinion and debate. It cannot be claimed that the law in relation thereto is in a satisfactory state, and obviously it is not to the law—law made by lawyers without the assistance of accountants—that we can look for any permanent solution.

The following extracts from various judicial decisions will suffice to confirm these observations—

"There is no law which prevents a company from sinking its capital in the purchase or construction of a money-making property or undertaking and from dividing the money annually yielded by it, without preserving the capital sunk so as to be able to reproduce it intact either before or after the winding-up of the company. When it is said, and said truly, that dividends are not to be paid out of capital, the word capital means the money subscribed pursuant to the Memorandum of Association, or what is represented by that money. Accretions to that capital may be realised and turned into money which may be divided among the shareholders, as was decided in *Lubbuck v. British Bank of South America*."

"The Acts do not render it obligatory on a company which has lost some of its capital to reduce the nominal amount mentioned in its Memorandum of Association. There are advantages in doing so, and the Acts were passed to enable limited companies to obtain these advantages; but there is nothing in the Acts which prevents a company which has lost part of its capital from continuing to carry on business and declaring and paying profits."

"There is nothing in the Act which says that dividends are only to be paid out of profits, . . .

but still there is this firmly fixed, that capital assets of a company are not to be applied to any purpose not within the objects of the company, and paying a dividend is not the object of a company—the carrying on of the business of the company is its object. In considering whether this is to be treated as an honest division of profit or as a division of capital under the guise of declaring a dividend, the Court will have regard to the directions of the Articles of Association, although, of course, if these Articles authorise not a mere division of profit but a division of capital (using capital in the proper sense of the word, by which I mean permanent assets and assets not to be expended in providing for the profit earned by the company), such a provision will be *ultra vires* and void."

"Perhaps the shortest way of expressing the distinction which I am endeavouring to explain is to say that fixed capital may be sunk and lost, and yet that the excess of current receipts over current payments may be divided; but that floating or circulating capital must be kept up, as otherwise it will enter with and form part of such excess, in which case to divide such excess without deducting the capital which forms part of it will be contrary to law."

It may be added here that the term fixed capital is generally translated as property purchased or acquired, and intended to be retained and employed with a view to profit, and that circulating capital is interpreted as property either produced, purchased, or acquired with the view or object of sale at a profit.

"Where nominal share capital is diminished in value, not by means of any improper dealing with it by the company, but by reason of causes over which the company has no control, or by reason of its inherent nature, that diminution need not, in my opinion, be made good out of revenue. In such a case a dividend may be paid out of current annual profits arising from the excess of ordinary receipts over expenses properly chargeable to the Revenue Account, provided there is nothing in the Articles of Association prohibiting such an application of profit, and that it is done honestly. The Capital and the Revenue Accounts appear to me to be distinct and separate accounts and for the purpose of determining profits, accretions to or diminutions of the capital are to be disregarded."

"The broad question raised by this appeal (*Verner v. General and Commercial Investment Trust*) is whether a limited company, which has lost part of its capital, can lawfully declare or pay a dividend without first making good capital which has been lost. I have no doubt it can, that is to say, there is no law which prevents it in all cases and in all circumstances. Such a proceeding may sometimes be perfectly legal and

may yet be opposed to sound commercial principles. There is a vast difference between paying dividends out of capital and paying dividends out of other money belonging to the company and which is not part of the capital mentioned in the company's Memorandum of Association."

The Lord Chancellor in the case of *Dovey and Others v. National Bank of Wales*—

"I am very reluctant to enter into the question which, for the reasons I have given, does not arise here and into which the Court of Appeal has entered at some length. The only reason why I refer to it at all is lest by silence I should be supposed to adopt a course of reasoning as to which I am not satisfied that it is correct. I doubt very much whether such questions can ever be treated in the abstract at all. The mode and manner in which the business is carried on and what is usual or the reverse may have a considerable influence in determining the question what should be treated as profits and what as capital. Even the distinction between fixed and floating capital, which in an abstract treatise like Adam Smith's *Wealth of Nations*, is appropriate enough, may, with reference to a concrete case, be quite inappropriate. It is easy to lay down that you must not pay dividends out of capital but the application of that very plain proposition may raise questions of the utmost difficulty in their solution. I desire, as I have said, not to express any opinion, but as an illustration of what difficulties may arise, the example given by counsel of one ship being lost out of a considerable number and the question whether all dividends must be stopped until the value of the lost ship is made good out of further earnings of the company or partnership, is one which one would have to deal with. On the other hand, people put their money into a trading concern to give them an income, and the sudden stoppage of all dividends would send down the value of their shares to zero and possibly involve its ruin. On the other hand, companies cannot, at their will and without the precautions enforced by statute, reduce their capital; but what are profits and what is capital may be a difficult and sometimes almost impossible problem to solve. When the time comes that these questions come before us in a concrete case, we must deal with them; but until they do I, for one, decline to express an opinion not called for by the particular facts before us, and I am the more averse to doing so because I foresee that many matters will have to be considered by men of business which are not altogether familiar to a court of law."

Ely, in his *Outlines of Economics*, divides the term gross profits into—

- (a) replacement for wear and tear, or fund for depreciation;
- (b) insurance against risk or reserve fund;

- (c) interest on capital;
- (d) wages of superintendence;
- (e) pure profit, being the reward of exceptional ability or opportunities in production.

In some French companies, it may be here stated that the French investor has his return divided into—

- (a) *intérêt statulaire*;
- (b) *dividende*.

Economic profits, commercial profits, and legal profits are quite distinct factors. Moreover, there are various degrees of commercial profits, and it would be a comparatively easy task to demonstrate that thousands of pounds representing so-called divisible profits are paid away in the shape of dividends that are not profits at all.

None of the decisions from which we have quoted can or should be taken as a standard, or as containing much in the way of principle that is not well known and that can be applied to cases generally.

Circulating assets must be maintained—that is merely an elementary expression of common-sense. Adequate provision should also be made in respect of machinery, plant, building, and other similar descriptions of property, even though they be fixed assets, or assets purchased with the subscribed capital of the company. For the most part they are merely payments in advance on account of revenue. There can be no true profit until after due provision has been made on account of the factors or elements which have contributed to earn the profit. Within the past two years a decision was given by one of the High Court Judges in the course of which he submitted that no profit could be deemed a true one until after provisions had been made for depreciation.

So far as the directors, secretaries and accountants of public companies, as well as the auditors, are concerned, they must consider each case in the light of the particular circumstances, and in such consideration they should have particular regard to the constitution and objects of the company, or its Memorandum and Articles of Association, and the accounts as a whole. If the auditor is dissatisfied or holds contrary opinions in any particular case, he may give expression to his dissatisfaction and his views in the course of his report to the shareholders. (See also AUDITING, p. 84.)

PROFITS, INTER-DEPARTMENTAL.

(See DEPARTMENTAL ACCOUNTS.)

PROFITS PRIOR TO INCORPORATION.

This matter arises when an incorporated company is formed and takes over the business from

a date anterior to the date of its incorporation. Obviously, as the company does not come into existence until it has received its certificate of incorporation, and in the case of a public company, is not entitled to commence business until it receives its trade certificate, it cannot earn profits before that date. Consequently the profits applicable to the period between the date the business is taken over and that on which the company is entitled to trade are not profits available for dividends, and they require special treatment. The method of arriving at the profits prior to incorporation depends on circumstances. If it is possible and not too inconvenient to take stock and prepare accounts up to date of incorporation, the amount of profit will be readily ascertained. As a rule, however, this is not feasible, and a method of estimating is generally adopted. In some cases the estimate is based on turnover, and in others on time. For example, suppose the company is incorporated on the 1st July to take over the business on the basis of the last Balance Sheet, which was made up on the preceding 1st January. The profits for the twelve months ended 31st December are £8,000, and the turnover for the same period £60,000. Adopting the turnover method, a reference to the books would show the turnover for the pre-incorporation period. Assuming this to be £25,000, the profits

prior to incorporation would be $\frac{25,000}{60,000} \times 8,000 = £3,333$; and the profits since incorporation £4,667. If the time method were used, the total profits would in this instance be divided into two equal portions, representing respectively amounts applicable to the pre-incorporation period and the post-incorporation period. There are obvious objections to both these methods, but they are, generally regarded as being sufficient for practical purposes. The profits prior to incorporation are as stated above, Capital Profits, and not available for dividends; and they are either kept as a Premiums' Capital Reserve, or used for the writing down of Goodwill or any of the fixed assets originally acquired by the company. In fact, such profits are really included in the purchase price, and the writing down of the fixed assets originally acquired is equivalent to reducing the purchase price.

PROFITS, UNDISTRIBUTED.

(See ACCOUNTS, CRITICISM OF, p. 24.)

PROHIBITION.

Just as in the case of mandamus (*q.v.*) a court of superior jurisdiction can compel a court of inferior jurisdiction to do a certain act which it has refused to do, so a similar power exists to

restrain the carrying out of something which ought not to be done. This is called "prohibition." For example, a County Court Judge may make an order which is beyond his legal powers. If he does so, an application may be made to a Divisional Court of the High Court of Justice to forbid him acting in the matter.

PROMISSORY NOTE.

By the Bills of Exchange Act, 1882, a promissory note is defined to be "an unconditional promise in writing made by one person to another signed by the maker, engaging to pay, on demand, or at a fixed or determinable future time, a sum certain in money to, or to the order of, a specified person or to bearer." There is no prescribed form, but the promissory note generally runs as follows—

"London, January 1st, 19..

"£100.

"Three months after date I promise to pay to Mr. John Brown or order the sum of one hundred pounds, for value received.

"Joseph Smith."

The modifications as to time of payment, order or bearer notes, indorsement, etc., in the case of bills of exchange are applicable to promissory notes.

In the above example, Joseph Smith is called the "maker," and John Brown is the "payee" of the promissory note. The liability of the maker of a promissory note corresponds to the liability of the acceptor of a bill of exchange. The payee and each indorser occupies the same position under both documents; but no person is liable to be called upon for payment until the note has been presented to the maker at the proper time and until payment has been refused by him.

If a promissory note is signed by two or more persons it is called a joint and several note, and each of the parties who signs it is liable to be sued by the holder if payment is not made in due course.

A promissory note must in some cases be presented for payment with due formalities, and it must not be allowed to remain unrepresented for an unreasonable time. What is an unreasonable time is a question of fact depending upon the circumstances of the case.

The stamp on a promissory note, which must be an impressed one, is the same as on a bill of exchange, except that the duty is always *ad valorem*, and not reduced to 2d. when the promissory note is made payable "at sight," or "on demand," or within three days after date or sight, or demand.

PROOF OF DEBTS IN LIQUIDATION.

(See LIQUIDATORS, ACCOUNTS OF, p. 679.)

PROOF OF DEBTS IN WINDING UP.

(See LIQUIDATORS, ACCOUNTS OF, p. 679.)

PROPERTY.

This word is of almost indefinite extent, and includes every species of thing in which a person may have an interest. (See also AUDITING, p. 96; BANKRUPTCY ACCOUNTS, p. 171.)

PROPERTY, AFTER-ACQUIRED.

(See AFTER-ACQUIRED PROPERTY.)

PROPERTY DIVISIBLE AMONG CREDITORS IN BANKRUPTCY.

(See BANKRUPTCY, PROPERTY DIVISIBLE AMONG CREDITORS IN.)

PROPERTY NOT DIVISIBLE AMONG CREDITORS IN BANKRUPTCY.

(See BANKRUPTCY, PROPERTY DIVISIBLE AMONG CREDITORS IN.)

PROSPECTUS, AUDITORS AND.

(See AUDITING, p. 70.)

PROSPECTUSES.

A prospectus is defined by Section 285 of the Companies (Consolidation) Act, 1908, as "any prospectus, notice, circular, advertisement, or other invitation offering to the public for subscription or purchase any shares or debentures (including debenture stock) of a company." The important phrase in this definition seems to be the expression "offering to the public." The question as to what is an offer to the public can be answered only by reference to the facts of each particular case. Thus, for example, an offer of shares in a newly reconstructed company to members of the old company is not an offer to the public, nor is an offer to existing shareholders or debenture holders. Generally speaking, it would seem that an offer to the public would include any offer to all persons who may choose to take shares. The offer must have been made by the company and not by an unauthorised individual.

FORMALITIES NECESSARY.—It is very important that it be made clear in the case of any document whether or not it is truly a prospectus. If it is decided that a circular or notice is a prospectus, it is then necessary for it to comply with the conditions laid down in the Companies Act, particularly Sections 80 and 81. Under Section 80 it is necessary that every prospectus shall be dated, and the date on the document is the date of publication. It is further necessary to register a copy of the prospectus with the Registrar of Joint Stock Companies on or before the date of publication. Until a copy signed by every person named

in the document as a director or proposed director has been filed for registration no copy of the document should be issued. Before issue, the prospectus should bear on its face a statement that it has been filed for registration in accordance with the requirements of the Act. The foregoing duties in relation to a prospectus are those of the secretary rather than of the auditors of the company. The auditor, however, is to a certain extent interested in the prospectus of a normal company. His name generally appears on the face of it, and Section 81 expressly lays down that amongst other things the prospectus must state the names of the auditors (if any) of the company. The mere fact that the auditor's name appears on the face of the prospectus or in the particulars required to be shown under Section 81 does not make the auditor a person responsible for the issue of the prospectus. As auditor he is merely a servant of the company, and he will not be responsible for statements in the prospectus unless he has actively participated in them, as, for example, by giving financial details in respect of the company.

PARTICULARS IN A PROSPECTUS.—Section 81 of the Companies Act, 1908, lays down in detail the requirements with which the prospectus shall comply. It must show—

1. The contents of the Memorandum of Association showing the names, descriptions, and addresses of the signatories and the number of shares subscribed for by them, together with a statement as to the number of founders, management, or deferred shares, and the interest of the holders thereof, in the company and its property;

2. The qualification shares of a director as fixed by the articles and any provision for remuneration;

3. The names, descriptions, and addresses of directors;

4. The minimum subscription on which directors may proceed to allotment, showing the amount payable on application and allotment; and, in the case of a second allotment, showing the amount of capital offered for subscription, and the amount taken up on each allotment during the previous two years;

5. The number and amount of shares and debentures issued within the two years previous as fully or partly paid otherwise than in cash, together with the statement of the consideration (see RETURN OF ALLOTMENTS);

6. The names and addresses of the vendors of any property to be acquired by the company and to be paid for out of the proceeds of the issue of shares offered by the prospectus, or of any property the acquisition of which has not been completed at the date of the prospectus. The prospectus. The prospectus must also state under this head the amount payable in cash, shares, or debentures to the vendor or vendors;

7. The amount of purchase money paid or payable in cash, shares, or debentures for any such property, showing the amount payable for goodwill separately;

8. The amount paid during the preceding two years as commission for subscribing for or procuring subscriptions for shares in or debentures of the company, and particulars of the rate of such commission. Commissions payable to sub-underwriters do not need to be disclosed;

9. An estimate of preliminary expenses;

10. The amount paid within the two preceding years or intended to be paid to a promoter, and the consideration for the payment;

11. The dates and the names of the parties to every material contract, and a reasonable time and place at which the contract or a copy thereof may be inspected. Contracts in the ordinary course of business or those made more than two years before the prospectus was issued need not be stated;

12. The names and addresses of auditors (if any);

13. Full particulars of the interest of any director in the promotion of or in the property to be acquired by the company, with a statement of all sums paid or to be paid to him in cash, shares, or otherwise, by any person, either to induce him to become a director or to qualify him as such, or otherwise for services rendered by him or his firm in connection with the promotion or formation of the company; and

14. Where the company has more than one class of shares, the voting rights of the various classes should be distinguished.

RESPONSIBILITY FOR ISSUE.—Where a prospectus is published in a newspaper, it is not necessary to state the contents of the memorandum, and if it is issued more than a year after the commencement of business, the first three requirements, the statement of preliminary expenses and the particulars as to a director's interests in the property of the company may be omitted. There are no penalties laid down for failure to comply with the above requirement as to a prospectus, but no doubt directors and other officers responsible would be liable for a misfeasance and also for damages at the suit of a shareholder injured. Any person responsible for the issue of a prospectus may escape liability arising out of non-compliance if he proves that he was not cognizant of the particulars not disclosed, or that the default was due to an honest mistake of fact.

Formerly, a company and an applicant for shares could contract out of the liability which might be incurred by failure to comply with the requirements as to disclosures in a prospectus, but under the Act of 1908 this is impossible. Further, it should be remembered that fraudulent failure to comply with Section 81 would possibly be good ground for criminal prosecution.

In addition to the points that it is necessary to disclose, the Companies Act,¹ 1908, by Section 84, provides against fraudulent statements and simple misrepresentations of fact. Under this section a director or other person responsible for the issue of the prospectus is responsible for the truth of the statements he makes, and will be liable in an action for damages should the statements prove to be untrue. Such persons can evade responsibility in the following cases, namely, where they

1. Have an honest and reasonable belief in the truth of the statement; or

2. Rely on the authority of some official person or document, or of some expert reasonably believed to be competent; or

3. Have withdrawn consent to act as a director before the issue of the prospectus; or

4. Had no knowledge of the issue of the prospectus and repudiated it on becoming aware of it; or

5. Had discovered the misrepresentation and withdrawn consent to the documents, giving public notice of the fact.

Quite apart from Section 84, any untrue statement in a prospectus would entitle the subscriber for shares on the faith of the prospectus to apply to the Court for a rescission of his contract.

PROTECTED TRANSACTIONS.

It is the policy of the bankruptcy law to divide the whole of the available property of the bankrupt rateably amongst his creditors. From the moment of the making of the receiving order against him the debtor is divested of all property with certain small exceptions, and he is theoretically incapable of acquiring anything for himself until he has obtained his discharge. Similarly, in the case of certain transactions which took place prior to the making of the receiving order, the law will afford no protection to the transferees of property by the bankrupt. Thus, if the bankrupt has made a voluntary settlement, that is, one for which there is no valuable consideration, however "good" the consideration may be, the settlement is absolutely void if made within two years, and it is voidable if made within ten years, unless the bankrupt is able to prove that he could at the time of the making of the settlement pay the whole of his debts without the aid of the property comprised in the settlement. (See **VOLUNTARY SETTLEMENT**.) But settlements or conveyances of property, if made *bonâ fide*, and for valuable consideration are always protected, that is, the transferee obtains a good title as against the Official Receiver or the trustee. And if, during the bankruptcy, the debtor has property in his possession and transfers it to a person *bonâ fide* and for valuable consideration, this is also protected. Until recently this protection was only given in the case of a transfer of personal property,

but now, by the Bankruptcy Act, 1914, the rule applies to real property as well as to personal.

PROTESTING A BILL OF EXCHANGE.

(See BILL OF EXCHANGE, PROTESTING.)

PROVING THE BALANCES.

(See BALANCES, PROVING THE.)

PROXY.

This term is applied either to the person who acts on behalf of another, or to the deed or document under which a person is deputed to act. It will be seen, therefore, that a person who is a proxy is a kind of agent, appointed to act for his principal in some special manner, in fact, he is a particular agent. The most common instances of one person acting for another in this way are in the cases of company meetings or of bankruptcy proceedings. The regulations as to the former are set out in the Deed of Settlement, Private Act of Parliament, or (in the case of a limited company) in the Articles of Association of the company; and as to the latter, the Rules under the Bankruptcy Act, 1914, must be consulted.

Section 68 of the Companies (Consolidation) Act, 1908, gives power to a company which is a member of another company, by resolution of the directors, to authorise any of its officials or any other person to act as its representative at any meeting of the other company, and to exercise the same powers on behalf of the company which he represents, as if he was an individual shareholder of the other company.

The instrument appointing a proxy, in the case of a company meeting, must be deposited at the registered office of the company within the time specified in the articles.

The following is a common form of a proxy in the case of a limited company—

Company Limited.

I of in the county of
 being a member of the Company,
Limited, hereby appoint of as
my proxy to vote for me and on my behalf at the
[ordinary or extraordinary, as the case may be]
general meeting of the company to be held on
the day of and at any
adjournment thereof.
Signed this day of

A person may be appointed proxy for one occasion only or generally. If for one occasion, the stamp duty is one penny. If generally, a stamp of 10s. is required. No stamp is required when the proxy is one which is used in connection with bankruptcy proceedings.

PUBLIC AUDITS.

(See AUDITING, p. 54.)

PUBLIC COMPANIES, BOOKS OF REGISTRY.

(See AUDITING, p. 71.)

PUBLIC COMPANY AUDIT.

(See AUDITING, p. 67.)

PUBLIC EXAMINATION IN BANKRUPTCY.

(See BANKRUPTCY, PUBLIC EXAMINATION IN.)

PUBLIC POLICY.

Anything is said to be contrary to public policy which is deemed, according to the standard of morality of the time, to be detrimental to the interests of the public in general. No exact definition can be given of what the phrase covers, but it is not out of place to quote the words of Sir George Jessel, when Master of the Rolls, in the case of *Besant v. Wood*, 1879, 12 Ch.D. 605: "You cannot lay down any definition of the term 'public policy,' or say it comprises such and such a proposition, and does not comprise such and such another; that must be, to a great extent, a matter of individual opinion, because what one man, or one judge, and perhaps I ought to say one woman also, might think against public policy, another might think altogether excellent public policy. Consequently, it is impossible to say what the opinion of a man or a judge might be as to what public policy is." With the change of ideas and a relaxation in the generally accepted standard of morality, public policy has been much narrowed, and latterly there has been a general disposition on the part of our judges to refuse to express what it really covers.

PUBLIC TRUSTEE ACT, INVESTIGATION UNDER.

(See INVESTIGATIONS, p. 588.)

PURCHASE DAY BOOK.

(See INVOICE BOOK.)

PURCHASES ACCOUNT.

A Nominal Ledger Account for recording the total purchases of goods made by a trader. The account is debited with the periodical totals of the Purchases Book, and credited with those of the Outward Returns Book. At each balancing its balance represents the purchases actually made during the period under review, and is transferred from it to the debit of the Trading Account.

In the case of a business having departments, the Purchases Account may be kept in columnar form, giving the total purchases and their analysis of each department, the Purchases Book and Inward Returns Book being similarly arranged to give the information requisite for its compilation. (See also AUDITING, p. 79; SLIP SYSTEM OF POSTING; TRADING ACCOUNT, p. 917.)

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QUALIFIED ACCEPTANCE.

(SEE BILL OF EXCHANGE ; ACCEPTANCE.)

QUARTER DAYS.

The last days of each of the four quarters of the year upon which rent or interest becomes due, except as otherwise provided by the parties.

In England and Ireland the quarter days are—

(1) Lady Day, March 25th ; (2) Midsummer, June 24th ; (3) Michaelmas, September 29th ; and (4) Christmas, December 25th.

In Scotland the quarter days are—

(1) Candlemas, February 2nd ; (2) Whitsun, May 15th ; (3) Lammas, August 1st ; and Martinmas, November 11th.

QUASI PARTNER.

A person who is only a partner "in a sense." If, however, he act in such a manner as to lead the general public to infer that he is a member of the partnership firm, he is liable for the partnership debts on the doctrine of "holding out."

QUINQUENNIAL VALUATION.

For the purposes of making an assessment of the value of the property within the metropolis, which is the basis of rating, a valuation is undertaken once in every five years, and this is known by the name of the quinquennial valuation. The valuation list is invariably made out and settled before the 1st October, and it comes into force in

the following year on the 1st April. Unless there are very exceptional circumstances which call for the making of a supplemental list, the quinquennial valuation stands for five years, and any aggrieved ratepayer has no remedy at all during this period of five years if he has failed to make his objection at the time when the list was settled. The term is also applied to the actuarial valuation of the assets of those life assurance companies who have such a valuation made every five years for the purpose of arriving at the bonus to be either paid or credited to their policy-holders.

QUIT RENT.

(See CHIEF RENTS.)

QUITTANCE.

A discharge from a legal debt or liability.

QUORUM.

The minimum number of persons who are required to carry through or transact any particular business of any public body. The exact number is determined by the statute constituting the body, or by the regulations of the body itself. The question is one of importance in the case of public joint stock companies, and it is invariably provided by the Articles of Association—or by Table A of the Companies (Consolidation) Act, 1908—of what number of persons a quorum is to be formed.

RACK RENT.

THE full annual value of the land which is demised by a lessor to a lessee. It is, in fact, the highest rent which a tenant is willing to pay for the use and occupation of the land.

RAILWAY AUDIT.

(See AUDITING, p. 108.)

RAILWAY COMMISSIONERS.

These are the members of the special court established under the Railway and Canal Traffic Act, 1888, a court set up for the purpose of inquiring into questions connected with the application of the provisions of the various Acts of Parliament relating to railways and canals, such as the differences between the companies as to the joint working of their lines, and the allegations of private individuals against companies as to unfair charges or undue preferences. Some of the powers are now vested in Tribunals under the Railways Act, 1921. There is a Railway Commission for each of the three parts of the United Kingdom, and a judge is appointed to preside over each, the appointment being made for England and Wales, Scotland, and Ireland by the Lord Chancellor of England, the Lord President of the Court of Session of Scotland, and the Lord Chancellor for Ireland respectively. As knowledge of a practical character is always necessary in such inquiries, the judge is assisted by two Commissioners appointed by the Crown on the advice of the Board of Trade, one of these Commissioners being a person chosen to sit on account of his knowledge of the working of railways. The Commission sits like an ordinary Court, and its judgments have the same weight as any other judgments of any division of the High Court.

RAILWAYS, BALANCE SHEET OF.

(See BALANCE SHEET, p. 148.)

RATES AND TAXES.

It is advisable when recording the rates and taxes of a concern to open a distinct account for income tax, and another for the remainder of the taxes payable and the rates. The object of this is to arrive at the exact charge against profits for income tax, so that this sum may be written back when preparing the computation of the assessment to income tax, without having to analyse the Rates and Taxes Account to ascertain what proportion of this latter charge consists of income tax.

Rates and taxes are items which accrue from day to day, and the auditor must, therefore, take care that a proper reserve is made in the Balance Sheet for any accrued liability, or any portion of the charge which has been paid in advance in respect of these items.

It is also the duty of the auditor to satisfy himself that the assessments upon which the rates and taxes are levied are correct. Particular attention should be paid to the assessment to income tax, so that proper provision may be made in respect of any accruing liability under this head. Official receipts should be required in every instance in support of payments made for rates and taxes. (See also PROFIT AND LOSS ACCOUNT, p. 790.)

RATIFICATION.

Any act or series of acts by which an unauthorised action on the part of a person is adopted by another as his own. The term arises most commonly in connection with agency. Thus, an agent is appointed for a certain purpose and he is not allowed, *primâ facie*, to exceed the limits imposed upon him. If he does exceed these limits the principal is not liable. But if the principal in any way assents to what has been done, or adopts the transaction as his own, or retains the benefit (if any) accruing from the same, he is said to ratify the *ultra vires* action of his agent, and he is bound by it just as though he had authorised it.

RAW MATERIAL.

Material in the unmanufactured state, the state varying with the manufacture in which it is to be employed. Thus, to the iron smelter the ore, limestone, etc., are his raw materials, but to the ironfounder the pig iron is his raw material.

REAL ACTIONS.

One of the divisions of action at law is into real actions and personal actions, or into actions *in rem.* and actions *in personam.* The former are certain actions in the Admiralty Division, which, being instituted against the vessels themselves or other subject matter of the suit, definitively adjudicate as against the whole world upon the property in the vessels or other subject matter. Prior to the passing of the Real Property Limitation Act, 1833, there were many real actions in existence, in which the question as to the title of property was involved and not that of possession

only. These have now been abolished, and their place has been taken by the possessory action of ejectment.

REAL ESTATE.

One of the divisions of property is into real and personal, and real property (real estate or realty) includes all freehold—whether in fee simple, in fee tail, or for life—copyholds, and customary freehold lands. The equity of redemption (*q.v.*) is real estate, but leaseholds are personal estate. But where a will directs that real property shall be sold, it is reckoned as personal estate or property. The proper technical word to be used in a will when real estate is being given to a person is "devise." (See also LIQUIDATORS, ACCOUNTS OF, p. 650.)

REALISATION ACCOUNT.

(See PARTNERSHIP ACCOUNTS, pp. 760, 762.)

REALISATION OF ASSETS.

(See LIQUIDATORS, ACCOUNTS OF, pp. 648, 674.)

REALISED PROFITS.

Profits not only made, but actually received in cash.

REAL OR PROPERTY ACCOUNTS.

These are those other than Nominal and Personal Accounts, and comprise land and buildings, plant and machinery, stock, cash at bank and in hand, goodwill, investments, etc. They are, generally speaking, those of the assets of the firm other than amounts owing by debtors. (See below.)

REALTY.

(See EXECUTORSHIP ACCOUNTS, p. 448; REAL ESTATE.)

REBATE.

(See BALANCE SHEET, p. 142.)

RECEIPT.

The written acknowledgment of the payment of a sum of money. A receipt is always valuable as documentary evidence when a question arises as to whether money has been paid. But there

is no legal necessity for a receipt to be given by a creditor in respect of any debt unless the debtor demands the same, and even then the demand is not effective unless the amount in question is £2 and upwards.

By section 103 of the Stamp Act, 1891, it is provided—

"If any person

"(1) Gives a receipt liable to duty and not duly stamped; or

"(2) In any case where a receipt would be liable to duty refuses to give a receipt duly stamped; or

"(3) Upon a payment to the amount of £2 or upwards gives a receipt for a sum not amounting to £2, or separates or divides the amount paid with intent to evade the duty;

"he shall incur a fine of £10."

Under sections 101 and 102 of the Stamp Act, 1891, it is further provided—

"101. (1) For the purposes of this Act the expression 'receipt' includes any note, memorandum, or writing whereby any money amounting to £2 or upwards, or any bill of exchange or promissory note for money amounting to £2 or upwards, is acknowledged or expressed to have been received or deposited or paid, whereby any debt or demand, or any part of a debt or demand, of the amount of £2 or upwards, is acknowledged to have been settled, satisfied, or discharged, or which signifies or imports any such acknowledgment, and whether the same is or is not signed with the name of any person.

"(2) The duty upon a receipt may be denoted by an adhesive stamp, which is to be cancelled by the person by whom the receipt is given before he delivers it out of his hands.

"102. A receipt given without being stamped may be stamped with an impressed stamp upon the terms following; that is to say,

"Within fourteen days after it has been given, on payment of the duty and a penalty of £5;

"(2) After fourteen days, but within one month, after it has been given, on payment of the duty and a penalty of £10;

REAL ACCOUNT

Dr.						PLANT AND MACHINERY						Cr.					
19..						19..											
Jan. 1	To Balance b/d		£	s.	d.	Feb. 19	By Cash, Sale of Old		£	s.	d.						
Feb. 19	" Cash—New Machine		1,426	10	6		Machinery		100	0	0						
" 28	" " Belting		249	4	8		" Depreciation 10% p.a.		79	10	4						
			14	6	2	June 30	" Balance c/d		1,510	11	0						
			1,690	1	4				1,690	1	4						
19..																	
July 1	To Balance b/d		1,510	11	0												

and shall not in any other case be stamped with an impressed stamp."

The stamp on a receipt for £2 and upwards is 2d. The following documents are exempt under the provision of the Stamp Act, 1891—

"(1) Receipt given for money deposited in any bank, or with any banker, to be accounted for and expressed to be received of the person to whom the same is to be accounted for.

"(2) Acknowledgment by any banker of the receipt of any bill of exchange or promissory note for the purpose of being presented for acceptance or payment.

"(3) Receipt given for or upon the payment of any Parliamentary taxes or duties, or of money to or for the use of Her Majesty.

"(4) Receipt given by an officer of a public department of the State for money paid by way of imprest or advance, or in adjustment of an account, where he derives no personal benefit therefrom.

"(5) Receipt given by any agent for money imprested to him on account of the pay of the army.

"(6) Receipt given by any officer, seaman, marine, or soldier, or his representatives, for or on account of any wages, pay, or pension, due from the Admiralty or Army Pay Office.

"(7) Receipt given for any principal money or interest due on any exchequer bill.

"(8) *Repealed.* (See below.)

"(9) Receipt given upon any bill or note of the Bank of England or the Bank of Ireland.

"(10) Receipt given for the consideration money for the purchase of any share in any of the Government or Parliamentary stocks or funds, or in the stocks and funds of the Secretary of State in Council of India, or of the Bank of England, or of the Bank of Ireland, or for any dividend paid on any share of the said stocks or funds respectively.

"(11) Receipt indorsed or otherwise written upon or contained in any instrument liable to stamp duty, and duly stamped, acknowledging the receipt of the consideration money therein expressed, or the receipt of any principal money, interest, or annuity thereby secured or therein mentioned.

"(12) Receipt given for any allowance by way of drawback or otherwise of any goods or merchandise from the United Kingdom.

"(13) Receipt given for the return of any duty of customs upon a certificate of over entry."

Receipts upon a duly stamped letter of allotment or scrip certificate are exempt. The exemption is included in No. 11 (above).

The Finance Act, 1895, section 9, repealed exemption No. 8 in the Stamp Act, 1891, "Receipt written upon a bill of exchange or promissory note

duly stamped," and enacted that the duty shall be charged as if the exemption has not been contained in that Act, provided that neither the name of a banker (whether accompanied by words of receipt or not) written in the ordinary course of his business as a banker upon a bill of exchange or promissory note duly stamped, nor the name of the payee written upon a draft or order, if payable to order, shall constitute a receipt chargeable with stamp duty.

It has become a common practice for debtors to pay their accounts by cheques on which a form of receipt is indorsed. This form must bear a stamp and the stamp must be cancelled in order to make the receipt valid in law if the amount of the cheque is £2 and upwards.

RECEIPT BOOK.

A book of forms usually having counterfoils for the purpose of giving acknowledgments of the receipt of money to the payers.

RECEIPTS AND PAYMENTS ACCOUNT.

This is a statement frequently used by certain non-trading concerns; and shows, on the debit side, the actual receipts, and on the credit side the actual payment during the period covered by the account. It is, in fact, a summary of the cash book classified under suitable headings and includes items relating to capital as well as to income. (See also AUDITING, p. 103; PROFIT AND LOSS ACCOUNT, p. 783.)

RECEIPTS AND PAYMENTS, RECORD OF.

(See LIQUIDATORS, ACCOUNTS OF, p. 651.)

RECEIPTS, AUDITORS AND.

(See AUDITING, pp. 73 and 100.)

RECEIVER, APPOINTMENT OF.

(See RECEIVERSHIP ACCOUNTS.)

RECEIVERSHIP ACCOUNTS.

A Receiver may be defined as a disinterested person appointed to "receive" and be responsible for property, or the income arising from property. He may be appointed—

- (1) By the Court; or
- (2) Out of Court.

APPOINTMENT BY THE COURT.—A Receiver may be appointed by the Court—

- (a) In the case of a partnership dispute, to hold the property and assets of the firm until the question of ownership or distribution has been settled. Section 23 of the Partnership Act, 1890, empowers a judgment creditor of a partner to get an order for the appointment of a Receiver of the Partner's share in the partnership.

(b) Pending the hearing of a Probate action ; or pending the appointment of a legal personal representative ; or where waste or misconduct is proved against an executor or trustee. In such a case an executor forfeits his right of retainer over any assets that the Receiver may get in.

(c) As between a Mortgagor and Mortgagee, the Receiver being the Agent of the Mortgagor.

(d) On behalf of an infant or lunatic, to hold the estate until the disability of the true owner has been removed.

(e) On behalf of debenture holders in a company, when occasion arises to protect or enforce their security.

(f) As between debtor and creditor. A Receiver would be appointed in such a case where legal execution could not be obtained, such an appointment being known as appointment by way of "equitable execution."

(g) In all other cases where it seems just and convenient.

A Receiver may be appointed by the Chancery Division or by the King's Bench Division. A Receiver in Chancery is appointed to act pending the result of an action to determine the ownership of property, *e.g.* in a partnership dispute. Such a Receiver may be appointed in the course of an action, and is usually appointed as Receiver and Manager.

A Receiver in the King's Bench is one appointed *after* judgment, in cases where it is convenient or necessary to put the judgment into effect ; *e.g.* a receiver may be appointed to receive the rents and profits of real estate, and also of personal estate which by virtue of its nature cannot be reached by legal execution, *e.g.* a share in a partnership. Such a Receiver can never be a "Manager."

Who May be Appointed. Any disinterested person may be appointed ; occasionally one of the parties to the action is appointed, but only when he is willing to act without a salary. The Official Receiver may be appointed on application of creditors or debenture holders of a company. Where both Receiver and Liquidator are necessary the Court will, to save expense, usually appoint the same person to fill both offices.

The Court will not usually appoint a Receiver in partnership cases, unless the partnership has been dissolved, or some special grounds be shown, *e.g.* mismanagement endangering the whole concern. In case of dissolution of partnership, a receiver and manager may be appointed, to hold the assets until the business is sold. The Court leans to the appointment of one of the partners for this, unless there are good grounds to the contrary.

A person should not be appointed who is privileged against actions ordinarily enforceable against a Receiver, *e.g.* a Member of Parliament.

Rights of a Receiver. (1) *To act as an Officer of the Court.* Interference with the Receiver may be considered as contempt of Court.

(2) *Possession of the Property.* The order of appointment usually directs the parties to the action to put the Receiver in possession at a certain specified date.

The appointment of a Receiver takes the goods out of the "possession, order and disposition" of a bankrupt. A landlord may, with leave of Court, distrain, even though a Receiver be appointed.

(3) *To Remuneration.* There is no settled scale of salary or remuneration, each case being settled on its own merits. The remuneration is frequently fixed upon the passing of the first account, and in the case of rents collected, the percentage is usually 5 per cent. upon the amounts received. If large sums are involved, *e.g.* on realization, the allowance may be reduced to $1\frac{1}{2}$ per cent. or $2\frac{1}{2}$ per cent. as the circumstances may indicate.

A Receiver may be allowed an amount, in addition to his salary, for any extraordinary trouble or expense he may have been put to, *e.g.* bringing or defending actions, but as a general rule such allowance will *not* be passed unless the expenses were incurred with the approbation of the Court.

Powers of a Receiver. A Receiver has the power to do all such acts for the protection and preservation of the property as the owner himself could do if he were in possession, although it may be necessary in some cases to obtain the sanction of the Court. Application to the Court for sanction should be made by a party to the proceedings ; if he refuses, the Receiver should make the application. If the Receiver is a Receiver and Manager his powers would extend to such acts as are necessary for the management of the estate.

The Receiver may, without sanction of the Court, pay for ordinary small repairs and other expenses such as insurance, and grant leases for not exceeding three years. He should obtain sanction of the Court for heavy expenditure, and for granting longer leases than three years, as also for charging the property as security for borrowing money.

Duties and Liabilities of a Receiver. The duties and liabilities of a Receiver may be summarised as follows—

(1) *To give Security.* Unless otherwise ordered, the Receiver appointed by the Court must give security that he will account for his receipts and apply such receipts as directed. A professional accountant is frequently appointed, his security being obtained through a Guarantee Society. The amount of the security depends upon the sums that will come into his hands. The premium payable to the Guarantee Society is not allowed by the Court as a payment out of the estate.

Until the security is given, the Receiver cannot take possession.

(2) *To give Notice of Appointment.*¹ Where a Receiver is appointed of property of a company, the person obtaining the appointment must, within seven days after the appointment, give notice to the Registrar of Joint Stock Companies (Sec. 94, Companies (Consolidation) Act, 1908). The penalty for default is £5 a day.

(3) *To take Possession of the Property.* The Receiver should take over the keys, make the necessary arrangements with the Bank, and generally take physical possession, and make himself familiar with the position of the estate, so that he can conduct or care for it with such skill and diligence as he would exercise in his own affairs. He should investigate agreements and insurance policies, and see that they are maintained; pay all the usual rates, taxes, and other outgoings, and execute necessary small repairs. These things can be done without leave of the Court; but sanction should be obtained before incurring expenditure of considerable sums, otherwise the Receiver may find such expenditure disallowed when he presents his accounts. The Receiver should collect all the assets he can. In the case of refusal to deliver up property or pay debts to him, application should be made to the Court, as legal proceedings should not be taken without leave of the Court.

Where a Receiver is appointed by holders of debentures secured by a floating charge he must discharge preferential payments in priority to any claims for principal or interest in respect of such debentures (Sec. 107, Companies (Consolidation) Act, 1908).

Receiver to Keep and Deliver Accounts and Pay into Court Balances of Moneys due. *Delivery of Accounts.* The Receiver must deliver his accounts to be passed annually unless the Judge otherwise directs. The Order appointing the Receiver contains directions as to the passing of accounts, as follows—

"And it is ordered that the said (Receiver) do on the day of and on the same day in each succeeding period of , leave in the Chamber of the Judge his accounts, and do within fourteen days after the allowance of such account, lodge in Court the balance, which shall thereby be certified to be due from him on such account, or such part thereof as shall be certified to be proper to be so paid."

The account must be in the prescribed form, and accompanied by vouchers, which must be numbered to correspond to the numbering of the items in the Account. Erasures are forbidden. Petty Cash disbursements (under £2) should be shown in total, supported by the production of a

detailed schedule or Cash Book, a separate voucher for each of such items not being necessary.

Separate accounts must be lodged for receipts and payments in respect of personal estate and of real estate. On the first account of "rents" collected the Receiver must state "how each tenant holds," *i.e.* weekly, quarterly, or yearly tenancy, etc.

See Appendices A and B (p. 806) for form of accounts.

On the day appointed, the Receiver attends and leaves his accounts at Chambers, such accounts being verified by affidavit, and obtains an appointment for the passing of the accounts. If the Order of appointment so directs, the Receiver must leave a copy of the accounts with each of the parties interested in the action.

Passing the Accounts. All interested parties may attend the passing of the accounts. The Master may direct that only contested items need be brought before him, vouchers for the remainder being exhibited at the office of the Receiver. Vouchers need not be produced for items under 40s., these being verified by the Receiver's oath, but all other vouchers must be available, and the Receiver may be ordered to produce any documents required, which have come into his possession. After approval, the Master bases his certificate on the balance shown.

Surcharging Items in the Accounts. The Receiver may be cross-examined as to any item in the account. Any party wishing to surcharge an item must give notice of his intention, together with brief particulars of his claim.

Costs. The Receiver brings in his bill of costs, which, after being taxed, is included as a disbursement before the balance is struck.

Master's Certificate. The account on being passed is retained and filed by the Court, and a certificate as to the balance is given. Any items surcharged are enumerated (by reference to the numbers) on the certificate. After eight days the certificate becomes binding.

Payment of Balance into Court. Frequently the "lodgment schedule" is attached to the certificate, directing the Receiver to pay into Court the balance as shown in his account after deducting his remuneration and the taxed costs, and the Court fees payable on the account, less such sum as may be required for the payment of any liabilities. On attendance at the office of the paymaster, instructions will be issued as to the lodgment.

If the Receiver should at any time receive large sums of money, he should pay them into Court forthwith, to avoid the possibility of being charged interest.

Failure to Account. If the Receiver fails to lodge or pass any account, or to pay in balances at the time fixed, he may be required to attend

¹ It will be seen that this is a duty of the person obtaining the appointment, but the Receiver should see that it is carried out.

APPENDIX A

In the High Court of Justice, King's Bench Division
Mr. Justice.....

Between..... Plaintiff
and..... Defendant

The first account of....., the Receiver appointed in this action pursuant to the Judgment dated.....

No. of Item.	Date when received.	Names of Persons from whom received.	On what Account received.	Amount received.	No. of Item.	Date when paid or allowed.	Names of Persons to whom paid or allowed.	For what purpose paid or allowed.	Amount paid or allowed.
1	19.. Oct. 1	James Brown	Book Debt collected	£ s. d. 118 0 0	1	19.. Oct. 1	Ocean Accident Corporation.	Fire Insurance on Stocks lying at Bristol Docks, Three months to 31st Dec., 19..	£ s. d. 1 11 3
2	" 3	Henderson & Co. Ltd.	For sale of stocks	72 0 0					
3	" 7	Alex. Jones.	Book Debt collected	1315 0 0	2	" 30	Geo. Hooper	Brokerage at 1½% on Stocks sold	19 15 0
4	" 30	Lorne & Co.	For sale of balance of stocks at Bristol	174 0 0	3	Dec. 31	John Smith	Receiver's Remuneration	52 10 0
5	Dec. 15	Howell & Co.	Book Debt collected	£1682 1 0			Balance	Due from Receiver	1608 4 9
				£1682 1 0					£1682 1 0

APPENDIX B

No. of Item.	Date when received.	Names of Persons from whom received.	On what Account and in respect of what part of the Estate received and when due	Amount received.	No. of Items.	Date when paid or allowed.	Names of Persons to whom paid or allowed.	For what purpose paid or allowed.	Amount paid or allowed.
1	19.. Oct. 3	James Kerr	River Farm, in the Parish of Barnet, county of Middlesex. One Quarter's Rent to 29th September, 19.. (held on yearly tenancy expiring Christmas, 19..).	£ s. d. 35 0 0	1	19.. Sept. 29	Guardian Fire Office	One year's insurance to 29th Sept., 19..	£ s. d. 2 9 0
					2	" 30	T. C. Myer	Account for repairs to out-houses, at Home Farm	5 5 0
					3	Oct. 3	James Gill	Agent's commission for collecting rents of River Farm	1 15 0
					4	Oct. 3	James Kerr	5 per cent. of £35 Income Tax Schedule A.	15 0 0
					5	Dec. 31	X Balance	2nd instalment for 19.. paid 1st July, 19.. Receiver's Remuneration	3 3 0
				£35 0 0					7 8 0
				£35 0 0					£35 0 0

APPENDIX C ABSTRACT.

RECEIPTS.		PAYMENTS.	
£	s. d.	£	s. d.
To Proceeds of sale of Freshfold Factory Site at Wandsworth		By Preferential Claims	£ 300 0 0
" Liquidator of "The X Y Company, Ltd.,"	5,000 0 0	Remuneration of Receiver	315 0 0
Proceeds of call of 5s. per share on 20,000 Ordinary Shares	5,000 0 0	" Debenture Holders, Arrears of Interest	600 0 0
		Do Repayment of Principal	8,000 0 0
		" Liquidator of "The X Y Co., Ltd., Balance	785 0 0
	£10,000 0 0		£10,000 0 0

Signature..... Date.....

to show cause; further, he is liable to the disallowance of his remuneration; to be charged interest at the rate of 5 per cent. per annum on the balance not paid in; and to discharge from office and payment of costs.

APPOINTMENT OUT OF COURT.—In this case the Receiver is appointed by the parties (or some of them) themselves, without the intervention of the Court. The appointment is made either under power of appointment in an instrument when certain circumstances prescribed in the instrument have arisen, or by a special instrument, *i.e.* a Receivership Deed.

Probably the most common cases of appointment of a Receiver out of Court are—

(1) By Mortgagee under the Conveyancing Act, 1881.

(2) On behalf of Debenture holders in a company.

Receiver Appointed by Mortgagee under the Conveyancing Act, 1881. *Appointment.* In mortgages by deed made after 31st December, 1881, the mortgagee has implied power of appointing a Receiver where—

(a) There has been default for three months in complying with a notice to repay the principal moneys; or

(b) Interest is in arrear for two months; or

(c) Some other covenant has been broken.

The mortgagee can appoint a Receiver in writing under his hand, and remove him and appoint another in the same way. Under the Conveyancing Act, 1881, the Receiver is, unless otherwise expressly provided, the agent of the Mortgagor, but this is not implied in the case of a Receiver appointed by Debenture holders.

When a Receiver is appointed to the property of a company, notice of the appointment must be given within seven days, by the person making or obtaining the appointment, to the Registrar of Joint Stock Companies, who enters the notice in the Register of Mortgages and Charges. (Sec. 94, Companies (Consolidation) Act, 1908.) The penalty for default is £5 per day.

Rights and Powers. (a) *Remuneration.* The Receiver is entitled under the Conveyancing Act, 1881, to a commission, to cover remuneration and expenses, not exceeding 5 per cent. of the gross amount of all moneys coming into his possession, if so provided in the instrument of appointment. If the basis of his commission is not so fixed then the Court may, on his application, fix a rate at 5 per cent. or even higher.

(b) *To Sue and Distrain.* The Receiver may sue for income and levy distress in the name of the mortgagor or mortgagee.

(c) *To Indemnification.* The Receiver being an agent is entitled to be indemnified by his principal for his lawful acts.

In other respects the Receiver's Rights and Powers are derived from the Deed of Appointment.

Duties. (a) *Application of Moneys.* Receipts must be applied as follows—

(1) In keeping insured, if directed by the mortgagee in writing, the property comprised in the mortgage.

(2) In discharge of all rents, rates, taxes and out-goings affecting the mortgaged property.

(3) In keeping down all annual payments having priority to the mortgages in respect whereof he is Receiver.

(4) In payment of his commission, and of the insurance premiums payable under the Deed, and of proper repairs as directed in writing by the Mortgagee.

(5) In payment of the interest accruing due in respect of any principal money due under the Mortgage.

(6) To pay the residue to the person entitled.

(b) *To Keep and File Accounts.* There are no statutory requirements as to the accounts to be kept or lodged as in the case of a Receiver appointed by the Court, except as regards a Receiver of property of a company who, by Sec. 95 of the Companies (Consolidation) Act, 1908, is required every half-year, and on ceasing to act, to file with the Registrar of Joint Stock Companies an abstract, in the prescribed form, of his receipts and payments. The penalty for default is a fine not exceeding £50. (See appendix C (page 806) for specimen accounts.)

In every case, however, it is important that the Receiver should keep proper and careful accounts.

(c) *Notice of Ceasing to Act.* The Receiver of property of a company must file with the Registrar of Joint Stock Companies a notice that he has ceased to act, within twenty-one days of his so ceasing, and the Registrar will enter the notice in the register of mortgages and charges. The penalty for default is a fine not exceeding £50. (Sec. 95, Companies (Consolidation) Act, 1908.)

Receiver Appointed on Behalf of Debenture Holders in a Company. The implied powers under the Conveyancing Act, 1881, to appoint a Receiver do not apply to debenture holders. Unless, therefore, the Trust Deed contains specific power of appointment, application should, in case of default, be made to the Court for appointment of a Receiver. If the Receiver is appointed under specific clause of appointment in the Deed, the remarks above as to the appointment of a Receiver under the Conveyancing Act, 1881, apply, subject to any specific provisions in the Deed.

The conditions under which a Receiver may be appointed are usually endorsed on the Document of Charge, or contained in the Debenture Trust Deed, *e.g.* in the event of default in the payment of interest, or of any due repayment of all or part of the principal, or if the Company passes a valid resolution to wind up, or suffers a Receiver to be

appointed by the Court, it is apparent that the security of the Debenture holders is jeopardized, and the Trust Deed will usually provide that in such a case the whole amount becomes repayable forthwith, in which case the Debenture holders would exercise the right to appoint a Receiver.

Such a Receiver would have, *inter alia*, the following powers—

(1) To take possession of the property covered by the Charge.

(2) To carry on the business of the Company.

(3) To sell any of the property charged.

(4) To effect such a compromise as he considers to be in the interests of the Debenture holders.

Any surplus must be distributed *pari passu* to the Debenture holders.

It is usually declared in the Trust Deed, either expressly, or by the provision that Sections 19 to 24 of the Conveyancing Act, 1881, shall apply, that a Receiver appointed by the Debenture holders is to be the agent of the Company; in which case the Company, and not the Debenture holders, are responsible for his actions, or for his remuneration. In the absence of such a declaration, the Receiver will be regarded as the agent of the Debenture holders, who will consequently be liable for his acts and for his remuneration. The point is of some importance, as it will enable a Receiver to know who is responsible for his remuneration, and for his indemnity as regards any liability he may have incurred whilst carrying on the business.

Receiver Appointed by a Receivership Deed.

In the case of a Receiver appointed by a Deed, where neither the Conveyancing Act, 1881, nor the Companies (Consolidation) Act, 1908, applies, the appointment, rights, powers, duties and liabilities and accounts of the Receiver will depend on the Deed, and should be carefully set out therein. In all cases, careful accounts, minutes and other records should be kept, and professional advice taken in case of doubt.

Receivers and Income Tax. When a Receiver is called upon to pay interest or other annual payment, from which the payer is required to deduct income tax, he must deduct such tax, and give notice to the Inland Revenue, in order that an assessment may be made and the tax thus held in trust duly accounted for.

Receiver's Banking Account. The Bank Account should be in the name of the "Receivership" as if the Receiver deposits any moneys in a bank account in his own name, and the bank fails, he will be held responsible.

Receiver and Manager. A Receiver and Manager is appointed by the Court where, in addition to the getting in of income and property, a business has to be carried on and disposed of. As the usual reason for the appointment of a Manager is the sale of a business as a going concern, the Court

will not appoint a Manager of a statutory undertaking, which cannot be sold.

A Receiver and Manager is subject to the same regulations as a Receiver as regards appointment, rights, powers, duties, liabilities, etc.

A Receiver and Manager may be appointed out of Court by Debenture holders, if such power is contained in the Deed.

RECEIVING ORDER IN BANKRUPTCY.

(See BANKRUPTCY: RECEIVING ORDER.)

RECOGNISANCE.

This is the acknowledgment of the existence of a debt due to the Crown. Thus, when a preliminary inquiry takes place in a Court of Summary Jurisdiction, that is, the ordinary Police Court, and the case is sent for trial at the Assizes or at Quarter Sessions, the witnesses are bound over to appear and to give their evidence at the trial, and a bond is entered into, the amount of which is forfeited if the terms of the same are not fulfilled. Similarly, if a person goes bail for another, he is bound over in recognisances to produce the prisoner in due course for trial. Again, when a case is not of a serious character, a prisoner is sometimes bound over in his own recognisances to come up for judgment if called upon. Professional accountants and others, when appointed by the Court as liquidators of companies or receivers in the Chancery and King's Bench Divisions, have to enter into a recognisance. In each of these cases there is a debt due to the Crown which is enforceable immediately if the conditions of the bond are not fulfilled.

RECONCILIATION STATEMENT.

(See BANK RECONCILIATION STATEMENT.)

RECONSTRUCTION AND AMALGAMATION.

(See LIMITED COMPANY ACCOUNTS, p. 637; LIQUIDATORS, ACCOUNTS OF, p. 659.)

RECORD BOOK.

(See BANKRUPTCY ACCOUNTS, p. 187; LIQUIDATORS, ACCOUNTS OF, p. 651.)

REDDENDUM.

This is the name given to that clause in a deed by which the grantor reserves something to himself out of that which he has previously granted. In practice this clause is generally placed between the habendum (*q.v.*) and the covenants contained in the deed, and usually begins with the word "yielding" or "rendering." Thus, in a lease the reddendum is that clause which commences with the words "yielding and paying," and sets out what the lessee has to render out of the property to the lessor.

REDEMPTION OF DEBENTURES.

(See DEBENTURES.)

RED INK INTEREST.

(See ACCOUNT CURRENT.)

REDUCTION OF CAPITAL.

(See LIMITED COMPANY ACCOUNTS, p. 636.)

RE-EXCHANGE.

This is the name which is given to the loss resulting from the dishonour of a bill of exchange in a country other than that in which it was drawn or indorsed. By Section 57, Sub-section 2 of the Bills of Exchange Act, 1882, it is provided, "the holder (*i.e.* of a bill of exchange) may recover from the drawer or an indorser, and the drawer or an indorser who has been compelled to pay the bill may recover from any party liable to him, the amount of the re-exchange thereon until the time of payment." The mode of calculating the re-exchange is to ascertain the sum for which a bill at sight, at the prevailing rate of exchange, drawn at the time and place of dishonour, or the place where the drawer or the indorser resides, can be obtained, so as to produce at the place of dishonour the amount of the dishonoured bill, together with the cost of protest, the commission, the postage, and all other expenses in connection with the dishonour.

REFEREE.

In a general way a referee is a person to whom any question in dispute is referred for settlement. In law, he is most frequently mentioned in connection with arbitrations (*q.v.*), as he is the person who is selected by the parties to the arbitration to preside over an inquiry which is held where this mode of procedure is resorted to without the intervention of the Court. When, however, an arbitration is ordered by the Court, the case is sent to one of the three Official Referees, who are invested with many of the powers of a Judge of the High Court. (See ARBITRATION.)

REFEREE IN CASE OF NEED.

This is the name of the person to whom the holder of a bill of exchange may apply for payment in case the bill is dishonoured by non-acceptance or by non-payment. He must be named on the face of the bill, and must also consent to being named as referee, and such consent is signified by his signature being appended to words clearly setting out his position, such as, "In case of need apply to A B," or "In case of need with the A and B Bank, Liverpool." A referee, if named at all, is generally named as the guarantor for the stability of the acceptor of the bill, but if the bill is dishonoured for non-acceptance or for non-payment, a referee's name may be inserted as the guarantor of any other party to the bill, and he then becomes liable not

only to the holder but also to all parties subsequent to the party for whose honour he has accepted. (See BILL OF EXCHANGE: ACCEPTANCE FOR HONOUR.)

REGISTER OF CONTRACTS.

(See FINANCIAL HOUSES AND INVESTORS, ACCOUNTS FOR, p. 479.)

REGISTER OF DEBENTURE STOCK, AUDITORS AND.

(See AUDITING, p. 71.)

REGISTER OF DIRECTORS AND MANAGERS.

(See DIRECTORS AND MANAGERS, REGISTER OF.)

REGISTER OF INDUSTRIAL PLANT.

(See DEPRECIATION, p. 404; RENEWALS AND DEPRECIATION, p. 815.)

REGISTER OF MEMBERS, AUDITORS AND.

(See AUDITING, p. 71, MEMBERS, REGISTER OF.)

REGISTER OF MORTGAGES, AUDITORS AND.

(See AUDITING, p. 71.)

REGISTER OF SHAREHOLDERS, AUDITORS AND.

(See AUDITING, p. 71.)

REGISTER OF STOCKHOLDERS, AUDITORS AND.

(See AUDITING, p. 71.)

REGISTER OF TRANSFERS, AUDITORS AND.

(See AUDITING, p. 71.)

REGISTERED CAPITAL.

This refers to the nominal capital of a company, *i.e.* the amount of capital as set forth in the Memorandum of Association and in the Statement of Nominal Capital.

REGISTERED OFFICE, LOCATION OF.

(See MEMORANDUM OF ASSOCIATION.)

REGISTRATION FEES OF LIMITED COMPANIES.

The registration of a company is by no means a matter of cheapness. On the statement of nominal capital an *ad valorem* duty of 1 per cent. is payable and in addition the memorandum is chargeable with duty to a maximum of £50, but on a graduated scale of £2 up to £2,000, above £2,000 and up to £5,000 £1 per £1,000; for every £1,000 after the first £5,000 and up to £100,000 the rate is 5s., and 1s. per £1,000 over £100,000

to a maximum fee of £50, which is reached at £525,000. The following is a table of fees on various amounts of capital up to £1,000,000, and sufficient data is given to calculate fees on intermediate amounts.

TABLE OF FEES PAYABLE ON REGISTRATION

Share Capital as per Memorand'm.	Ad Valorem Duty on Statement of Capital.	Fee Stamp on Memorand'm.	Miscellaneous Fees.	Total Duty and Fees on Registration.
£	£ s.	£ s.	£ s.	£ s.
100	1 0	2 0	2 15	5 15
250	2 10	2 0	2 15	7 5
500	5 0	2 0	2 15	9 15
1,000	10 0	2 0	2 15	14 15
2,000	20 0	2 0	2 15	24 15
2,500	25 0	3 0	2 15	30 15
3,000	30 0	3 0	2 15	35 15
4,000	40 0	4 0	2 15	46 15
5,000	50 0	5 0	2 15	57 15
6,000	60 0	5 5	2 15	68 0
7,000	70 0	5 10	2 15	78 5
7,500	75 0	5 15	2 15	83 10
8,000	80 0	5 15	2 15	88 10
9,000	90 0	6 0	2 15	98 15
10,000	100 0	6 5	2 15	109 0
12,500	125 0	7 0	2 15	134 15
15,000	150 0	7 10	2 15	160 5
20,000	200 0	8 15	2 15	211 10
25,000	250 0	10 0	2 15	262 15
30,000	300 0	11 5	2 15	314 0
40,000	400 0	13 15	2 15	416 10
50,000	500 0	16 5	2 15	519 0
60,000	600 0	18 15	2 15	621 10
70,000	700 0	21 5	2 15	724 0
75,000	750 0	22 10	2 15	775 5
80,000	800 0	23 15	2 15	826 10
90,000	900 0	26 5	2 15	929 0
100,000	1,000 0	28 15	2 15	1,031 10
125,000	1,250 0	29 0	2 15	1,281 15
150,000	1,500 0	31 5	2 15	1,534 0
200,000	2,000 0	33 15	2 15	2,036 10
250,000	2,500 0	36 5	2 15	2,539 0
300,000	3,000 0	38 15	2 15	3,041 10
400,000	4,000 0	43 15	2 15	4,046 10
500,000	5,000 0	48 15	2 15	5,051 10
600,000	6,000 0	50 0	2 15	6,052 15
700,000	7,000 0	50 0	2 15	7,052 15
750,000	7,500 0	50 0	2 15	7,552 15
800,000	8,000 0	50 0	2 15	8,052 15
900,000	9,000 0	50 0	2 15	9,052 15
1,000,000	10,000 0	50 0	2 15	10,052 15

The miscellaneous fees include 10s. deed stamps on the Memorandum and on the Articles, and a 5s. fee stamp on each of the Articles, notice of situation of registered office, declaration of compliance with the Companies Acts, notification of director's consent to Act, list of persons who have consented to act as directors, copy of the register of directors, and file copy of prospectus or statement in lieu of prospectus. Private companies may deduct 15s. as the prospectus, list of consents, and notification of consent are not filed. Any other document requiring filing takes a fee stamp of 5s. which may be added to the foregoing total.

REGRET, LETTER OF.

Where no allotment is made to an individual applicant for shares, it is usual for a company to send a letter informing the applicant of the fact. Such a letter is known as a Letter of Regret, and takes the following form—

The X Y Company Limited.

L/R
No 214

Address of Registered Office,
Date

Sir, or Madam,

I am instructed by the Directors to inform you that they regret to be unable to make any allotment to you of the one hundred Ordinary Shares as applied for by you in your application of the 3rd March, 19... A cheque for £25 0s. 0d. attached hereto is the amount of your deposit which accompanied your form of application. Kindly sign the cheque in the space provided, and present it for payment without delay. No further acknowledgment of this communication is necessary.

I am,
Yours truly,
P. Q.
Secretary.

L/R
No. 214

LONDON,

.....19....

Stamp
2d.

To the Empire Bank, Ltd.

PAY to Mrs. Mary Jones, or order, the sum of twenty-five pounds.

For the X Y Company, Ltd.

R. S., Director.
P. Q., Secretary.

£25 0 0.

RE-ISSUE OF A BILL OF EXCHANGE.

(See BILL OF EXCHANGE, RE-ISSUE OF.)

RE-ISSUE OF FORFEITED SHARES.

(See LIMITED COMPANY ACCOUNTS, p. 633.)

RELATION BACK.

This is a doctrine in bankruptcy which has reference to the title of the trustee of the bankrupt to the property of the debtor. By the Bankruptcy Act it is provided that the bankruptcy of a debtor, whether it is on his own petition or on the petition of a creditor or creditors, shall be deemed to have relation back to, and to commence at, the time of the act of bankruptcy having been committed on which a receiving order (*q.v.*) is made against him, or, if the bankrupt is proved to have committed

more acts of bankruptcy than one, to have relation back to, and to commence at, the time of the first of the acts of bankruptcy proved to have been committed by the bankrupt within three months next preceding the date of the presentation of the bankruptcy petition. *Prima facie*, all transactions of the bankrupt after that time are void, and the title of the trustee in bankruptcy relates back to that time. (See section 37 of the Bankruptcy Act, 1914.)

REMAINDER.

The remainder in an estate is that interest which passes to a person or persons after the limited estates have been exhausted. Thus, if a life estate is granted to A, and after A's death the estate is devised to B in fee simple, B has what is called the remainder. If, instead of going to a third person, the grantor reserves the right in the estate to himself after the death of A—or after the extinction of A's estate in any other manner—this reservation is called the “reversion” (*q.v.*). The terms remainder and reversion are frequently, though improperly, used in the same sense. When it is absolutely certain that the estate must eventually become the property of the remainder-man, the estate is called a “vested remainder.” When the vesting depends upon the happening of some specified event, it is called a “contingent remainder.” (See also EXECUTORSHIP ACCOUNTS, p. 447.)

REMITTANCE ACCOUNT.

(See BRANCH ACCOUNTS, p. 269.)

REMOTE PARTIES.

Parties to a bill of exchange who are not immediately connected with each other in order of liability upon the instrument. Of course, every person whose name is lawfully upon a bill of exchange is liable in one way or another, if the signature is genuine or authorised. But the law makes a distinction between persons, for some are known as “immediate” and others as “remote.” Thus, the drawer and the acceptor, the acceptor and the payee, the payee and the first indorser, and any two indorsers whose names appear immediately after each other are “immediate parties.” But an acceptor and, say, a third or fourth indorser, are remote parties.

REMOVAL EXPENSES.

Generally speaking, the cost of removal of plant and machinery must be regarded as a part of the cost of maintaining the revenue-producing capacity of those assets, and, as such, must be charged against the Profit and Loss Account.

In certain circumstances, however, it may be argued that the cost of removal has not only

maintained the revenue-earning capacity of assets, but has actually increased that capacity, and, therefore, that this cost should be added to the capital value of the assets. Where the facts support this argument, the cost of removal may be temporarily capitalised and the cost spread over two or three years, particularly if it be a heavy one, and the balance at each period carried forward in suspense. The auditor should not, however, allow the expenses of removal to be permanently capitalised by adding it to the assets accounts without calling attention to it in his report. In any event, that portion of the removal expenses which applies to the cost of removing stock should be charged against the revenue of the period within which the expense is incurred.

RENEWAL OF BILL OF EXCHANGE.

(See BILL OF EXCHANGE, RENEWAL OF.)

RENEWALS AND DEPRECIATION.

It is necessary first to define what is meant by “Renewals” and “Depreciation.” “Renewals” may be taken to include the cost not only of replacing any item of capital expenditure, but also of the expenditure, *e.g.* repairs necessary to maintain that item in efficient working order during its lifetime. “Depreciation” includes the actual or estimated loss in value from any cause of buildings, plant and machinery, or furniture, and generally of such assets as are subject to loss in value by reason of wear and tear, or obsolescence, or otherwise, but which from their nature can only be valued approximately—the more exact methods of valuation available in the case of stocks on hand, securities, book debts and the like, being inapplicable.

It should be observed at the outset that certain assets—for example: buildings, which may be slowly but steadily depreciating from some cause such as wear and tear—may be equally, or even more quickly appreciating in value from some other cause, such as the rising cost of buildings of a similar type or an increased demand for accommodation in the district in which they are situated. Logically, as much attention should be given to appreciation as to depreciation, but the usual practice is to ignore the former (which therefore constitutes a secret or undisclosed reserve), or at most to let it operate as a diminishing factor when fixing rates of depreciation. Some points of considerable importance are involved in this practice of taking into account any loss while ignoring any increase in values. It is clear that any appreciation in the value of capital items represents a corresponding increase in the amount of the owner's capital. Such increase cannot,

however, be considered an earned profit, and still less a realised profit. On the other hand, as regards depreciation, there is the vital distinction that the loss may be due to one or both of two causes, viz.—

- (a) an actual use of the asset to earn a profit ;
- (b) some happening quite apart from such use.

In case (a) the profit earned should be charged with the loss in value of the asset used to earn such profit, for it is clearly a charge to revenue. In case (b) the loss is not usually charged against profits. Nevertheless the loss is a factor which must be taken into account if the true capital of the owner is to be ascertained. It is a loss of capital which, like all such losses not recoverable by insurance, can only be made good out of revenue if capital is to be maintained intact.

In appreciation, then, there is a gain which is clearly an increase of capital, whereas in depreciation there is a loss which may be a revenue charge or a charge to capital of partly one and partly the other. Further, in the case of appreciation, the gain, although it may be very real, cannot be said to be finally determined until it is realised ; but in the case of depreciation the loss may, according to its nature, be definitely known either wholly or in part.

The practice, therefore, of taking into account all depreciation, but leaving out of account any appreciation, is a prudent one, though as between two accounting parties it might operate unjustly, and therefore have to be brought into account in, for example, a dissolution of partnership.

The distinction between the two types of depreciation is a very important one in the case of joint stock companies, since the payment of dividends may be affected by it. The distinction is also important in connection with returns for income tax assessment and in the cost accounts of works.

Speaking generally, while it may be desirable to raise a special account for depreciation arising under case (b), such depreciation to be written off to revenue as opportunity occurs, or over a term of years, in most cases it is not legally necessary to do so before distribution of dividends out of profits or of income from a trust, subject in the latter case to the conditions of the trust.

In the case of individual traders or partners, such losses might be written off capital. A limited company, however, cannot write down its share capital by a stroke of the pen, and for this reason such losses are not infrequently ignored, unless the Articles of Association provide otherwise.

In all cases it is, however, necessary to make full provision for depreciation arising under case (a), and whatever the law may be it is a sound accounting principle to make adequate provision for both classes of depreciation, and it is on that basis that this article is written.

When devising methods to give effect in accounts to depreciation, steps must therefore be taken to ensure that sufficient allowance has been made for any decrease in the cost value of the assets which may have taken place between the date when they were acquired and the date of valuation or the balance sheet in which they are included. The most obvious way to ascertain the extent of the depreciation is to have a valuation of the assets in question made by expert valuers. This course is, however, rarely practicable. The cost in many cases would be prohibitive, and there would be a danger of too much weight being given to passing conditions. It is nevertheless most desirable that such valuations should be made at intervals of some years in order to test the accuracy of the means actually adopted. Usually the accountant will find that it is *his* duty to estimate or decide the provision for depreciation. For this purpose he must use his discretion after consulting all available opinion and authorities. From what has already been said it is evident that while an accountant should make every endeavour to estimate and provide, year by year, for depreciation, he can hardly hope to obtain strictly accurate results for any one year. The effects of depreciation can, however, be more closely determined by looking ahead over a term of years, and if the value of the assets at the end of the term can be estimated with some accuracy, the only question that can arise is whether the total allowances to be made for loss in value can be equally distributed over the period. The problem, therefore, is first how to estimate, as closely as may be, the probable loss in value of the assets under review over a period of years, and secondly to allocate that loss, as accurately as may be, year by year throughout the period. This is the whole problem so far as the financial accounts of an undertaking are concerned.

ANALYSIS OF DEPRECIATION.—When depreciation is analysed it will be found that, as already mentioned, it comes under one or other of the following headings—

- (1) Loss in value of asset arising from use.
- (2) Loss in value of asset not arising from use, but *e.g.* from such happenings as :
 - (a) Accident (not covered by insurance).
 - (b) Fall in purchase price of similar assets.
 - (c) Existence of a similar asset of greater efficiency.
 - (d) Existence of conditions tending to diminish or destroy the useful life of the asset.

Of the above, loss under heading (1), which covers all ordinary depreciation resulting from "wear and tear" is the most common and the most important, and is clearly chargeable to revenue.

As already indicated, loss in value not arising from use but falling under heading (2) cannot

strictly be regarded as a revenue charge, though it is prudent to provide for it out of revenue. Some examples will now be given of depreciation covered by the four sub-headings of (2). It will be found, however, that the distinction between the divisions and sub-divisions above set out is sometimes very fine.

(a) *Accident (not covered by insurance).*

This might include an almost endless variety of losses as to many of which it might be argued the loss arises from use. The following examples may be taken by way of illustration—

- (1) Sinking of ship (uninsured).
- (2) Breakdown of plant.
- (3) Destruction of property by earthquake, bombardment, etc.

(b) *Fall in purchase price of similar asset.*

It is evident that an asset loses in value if through the lapse of a patent, competition or any, other cause it can be purchased at less than the original cost price.

(c) *The introduction of a similar asset of greater efficiency.*

The loss in value in this case is generally described as depreciation due to obsolescence. For example, it is almost inevitable in any works that plant will have to be replaced from time to time by plant of a more efficient type if working costs are to be maintained at a competitive level.

(d) *Existence of conditions tending to diminish or destroy the useful life of the asset.*

This is another form of obsolescence due not to any loss of comparative efficiency in the asset but to exterior causes of which a change in fashion or taste may be taken as typical. For example, special plant set up for the production of some particular article may gradually or suddenly become of scrap value only, owing to the falling off in demand for the article. In many cases a limited demand can be anticipated when the plant is erected; as, for example, munition plant erected in war time. In such cases it is obvious that full allowance for the depreciation must be made and charged to the cost of production of the output.

RENEWALS.—The subject of “renewals” can conveniently be considered at this point, as it will be realised that the questions of depreciation and renewals are intimately connected. Renewals, as previously stated, include not merely replacements but also repairs. It is often argued that depreciation need not be considered if repairs are executed and replacements made whenever necessary, and the cost of both charged to revenue. The result would be that practically no charge would be made to revenue for the use of assets in the early years following their purchase, and that the assets would be over-valued except just after purchase or renewal. The argument, therefore, is unsound.

As a matter of practice it is the almost invariable rule to charge repairs to revenue and replacements to Capital Account. In this event it is only necessary that the allowance to be made for depreciation should be the difference between the price at which the asset is acquired and the estimated value of the asset at the date when its usual life is expected to cease, and this difference should be fairly distributed as a revenue charge year by year according to the estimated life of the asset.

The difficulties incidental to an estimate of this loss in value vary considerably according to the particular asset under consideration, and in many cases appear almost insuperable. By a careful classification of assets, however, much may be done to reduce the margin of error.

When charging repairs to revenue and replacements to Capital Account it is very important to see that the charges to Capital Account are strictly controlled. Particularly is this necessary in the case of large works carrying out their own renewals. In such cases special care must be taken to ensure that alterations and improvements, or partial renewal of the assets are not charged to Capital Account unless the replacement values of such assets have been increased to the extent of the charges. It is, of course, equally necessary to ensure that whatever the works cost may be the amount charged to Capital Account does not exceed the market value of the item so charged. To this end some writers suggest that only the bare cost of labour and materials used upon the replacement should be charged, but this exclusion of a proportion of manufacturing expenses is clearly inexact and suggests either unduly high working costs or untrustworthy cost accounts, or both.

GENERAL TREATMENT.—The general treatment of depreciation and renewals may now be considered on the basis that replacements will be charged to Capital Account. It will be convenient to review the methods available in a simple case since the principles will be the same under any conditions.

Assume that for the purpose of carrying out certain work fifty typewriters are purchased at £18 each.

Assume also that—

- (1) The life of a typewriter is estimated at seven years.
- (2) The residual value after seven years is estimated at £4 per typewriter.
- (3) The annual repair bill of each typewriter is estimated at 10s. for the first three years, 20s. for the next two years, and 30s. and 40s. for the sixth and seventh years.

It is then necessary to provide for a depreciation of £14 per machine over a term of seven years.

METHOD 1. The repairs may be charged to

revenue as they occur, and £2 per annum per machine to revenue for depreciation, crediting the depreciation amount either to the Typewriter Capital Account or to a Depreciation Reserve Account. This method is open to the serious objection that the total charge to revenue for repairs and depreciation is least when the machines are most efficient and gradually increases as they lose in efficiency.

METHOD 2. The estimated depreciation may be added to the estimated repairs and a charge of £3 per annum per machine made to revenue and credited to a Depreciation and Repairs Reserve Account, the repairs being charged against this account as they are incurred.

This method tends to make the annual charge more equitable, but the most efficient years of the machines are at best only charged at the same rate as the less efficient years. The method is, however, objectionable, because it necessitates estimates of both depreciation and repairs. Consequently it may be necessary at a later date to make adjustments for errors in two estimates instead of in the estimate for depreciation alone.

METHOD 3. Repairs may be charged to revenue as they occur, and a yearly charge made to revenue for depreciation of such a percentage of the cost value of the typewriters, less depreciation, if any, as will reduce them to a value of £4 each at the end of seven years. The percentage in this case would be 19·335. This method is the one which is almost universally adopted. It has the advantage that the depreciation charge becomes less and less as the repairs charge may be expected to increase. Whether in the final result the combined charge for depreciation and repairs for the earlier years of the asset is rather heavier than for the later years will of course depend upon the incidence of the repairs.

In the case chosen as an example it might be possible to arrange for the vendors to guarantee an allowance of £4 per machine at the end of seven years and also to contract for repairs either at a flat rate or upon an ascending scale for the whole period. In such an event it would clearly be possible so to calculate the revenue charge for depreciation and repairs that it would diminish, say, by 2 per cent. for each year (to allow for diminishing efficiency of machines), but would be such that the total charge to revenue for the seven years would exactly provide for the known repairs and depreciation. In practice such exactitude would be rarely, if ever, practicable. Both the useful life and residual values of assets are difficult to estimate, and only a close approximation is possible. Consequently rates such as 20 per cent., 15 per cent., 10 per cent., calculated on the diminishing values, should be chosen so as to leave at the end of a term of years values approximately equal to the estimated residual values.

Methods other than those mentioned could obviously be devised, *e.g.* varying combinations of the constant and diminishing depreciation charge methods, but, in general, method 3 is found to give results as satisfactory as can reasonably be expected.

The following tables show the annual charges to revenue as they would appear under methods 1 and 3 in the particular case taken as an example—

Year.	METHOD 1			METHOD 3		
	Depreciation.	Repairs.	Total.	Depreciation.	Repairs.	Total.
1	100 0 0	25 0 0	125 0 0	174 0 4	25 0 0	199 0 4
2	100 0 0	25 0 0	125 0 0	140 7 5	25 0 0	165 7 5
3	100 0 0	25 0 0	125 0 0	113 4 7	25 0 0	138 4 7
4	100 0 0	25 0 0	125 0 0	91 6 9	25 0 0	116 6 9
5	100 0 0	50 0 0	150 0 0	73 13 6	50 0 0	123 13 6
6	100 0 0	75 0 0	175 0 0	59 8 7	75 0 0	134 8 7
7	100 0 0	100 0 0	200 0 0	47 18 10	100 0 0	147 18 10
	£700 0 0	350 0 0	1050 0 0	700 0 0	350 0 0	1050 0 0

The question of depreciation may now be considered in relation to the assets most commonly met with in practice. No definite rules can be laid down as conditions affecting depreciation are constantly changing. Consequently such rates as are mentioned must be taken as susceptible to considerable variation.

To prevent any misunderstanding it is to be noted—

(1) That renewals will be dealt with on the basis that all repairs are charged to revenue as they occur and that replacements are charged to Capital Account.

(2) That all depreciation will be taken into account and charged to revenue. As already explained, it is, however, admitted that some depreciation does arise which can properly be charged to capital. Such intermittent and exceptional depreciation, even if charged to revenue, should not be considered in works accounts as a charge forming part of the cost of manufacture. For example, the loss arising from the collapse of a works building need not, at any rate in the first instance, be charged to revenue, but if charged it should not be allowed to enter into the manufacturing expenses and thus into the cost of the works output, since it would upset all ordinary calculations of costs or periodical statements of a comparative nature.

(3) That such rates as are quoted are percentages on diminishing values.

Land, Freehold and Leasehold Premises.

(a) *Land.* Usually no depreciation is charged in respect of land or on roads when charged to Lands Account. Fencing, if charged to Lands Account, should be kept distinct from the land and roads and depreciated according to type, say 5 per cent. for iron fencing.

(b) *Freehold Premises.* Depreciation will depend upon the construction, whether brick, iron, etc., and upon the nature of the trade carried on in the buildings and the state of repair in which the buildings are kept, and even upon climatic conditions.

Rates may vary from 1 per cent. to $2\frac{1}{2}$ per cent. when conditions are favourable.

(c) *Leases and Leasehold Premises.* The consideration for a lease often consists of a sum down and some liability at the end of the lease for dilapidations or by reason of some covenant in the lease. These two sums represent rent, *i.e.* rent payable in advance and deferred rent. It is necessary to spread such payments equitably over the term of the lease. The annual rent will be the annuity for the term of the lease which at a suitable rate of interest, say 5 per cent., can be purchased for the sum paid down at the commencement and the sum estimated as payable, *i.e.* the estimated liability, at the end of the lease.

It is quite wrong to describe this rent, as is frequently done, as the annual depreciation of the lease. Depreciation in leasehold property is the loss in value of the property due to the falling off in its letting value. If, however, the Lease Account be credited and Rent Account be debited with interest at the assumed rate upon the balance of the Lease Account, no further entry for depreciation need be considered, as full provision will have been made for the writing off of the Lease Account by the end of the lease. It should be noted, nevertheless, that the difference between the annuity and the letting value of the premises, if lower, represents not rent but depreciation.

In all these cases (a), (b) and (c), the distribution of the depreciation charge will cause no difficulty in, for example, Works Accounts. It will be allocated departmentally or otherwise, in exactly the same way as rent.

Plant. Plant in most works is analysed under two main headings—

- (1) Fixed plant.
- (2) Loose plant.

These classifications are, however, by no means rigidly adhered to. In general, all the more important and expensive pieces of plant are included in the first class, while in the second are included the less important items which cannot conveniently be recorded in a Plant Register as separate pieces of plant. Both classes will be subdivided according to the particular requirements of the works. Generally there would first be a sub-division of the plant according to its nature, and then a further sub-division departmentally. As an indication of the first sub-division of fixed plant the following will serve as examples.

Power Plant. Boilers, economisers, superheaters, engines, motors, turbines, etc.

Transmission Plant. (a) Mechanical—Chain transmission, shafting, etc.; (b) Electrical—Cables, switchboards, etc.

Transportation Plant. Cranes, lifts, motor vans, etc.

Manufacturing Plant. Lathes, sawing machines, printing presses, looms, vacuum pans, etc., etc.

In the case of loose plant the sub-division will, still more than in the case of fixed plant, depend upon the manufacturing processes carried on by the particular works, but there will usually be no great difficulty in grouping all loose tools, utensils, implements, and small plant into convenient classes.

The Register of Plant, referred to above, is an important preliminary to the fixing of depreciation rates in the case of important works. Usually a card is allotted to each important piece of plant, and provision is made upon the card for a full description of the plant with initial cost, details of additions to the plant and their cost, and for the depreciation rate. Space is also usually provided for recording all repairs and their cost, and the annual value of the plant after effect has been given to depreciation, that is to say, the value at which the plant is included in the Balance Sheet of the undertaking. Finally each piece of plant is allotted a distinctive number in the Register, and this number is affixed to the plant itself.

These cards can be readily sorted (a) in accordance with the class of plant and (b) departmentally.

The information provided by the cards gives a complete history of each class and piece of plant, and enables suitable rates to be more easily determined, and it becomes an easy matter to arrive at the total depreciation charge for each department of the works.

The cards comprising the Register, so far as capital values and depreciation entries thereon are concerned, are usually subsidiary to a Plant Account in the Works Ledger with which they have to agree in total.

Rates of depreciation for nearly all important classes of plant vary within very considerable limits, according to circumstances, but there have now been recorded, in one form or another, many rates which are thought to be satisfactory in the case of engineering, printing, chemical and other industries, and these records should be consulted.

In this connection it is important to remember that the still too frequent method of depreciating important plant values by the use of an average rate is unsatisfactory because, in the first place, the total depreciated plant value is not likely to be so accurate as when a rate is chosen for each piece or type of plant, and secondly because the allocation of the depreciation, which will

become necessary when works departmental costs are required, may be rendered seriously inaccurate.

The less important plant of a works consisting of all kinds of utensils, apparatus, etc., required in the manufacturing processes should, when practicable, be inventoried and valued, and should not be subject to any fixed rate of depreciation. In those cases where an actual stocktaking is found to be impracticable the loose plant, utensils, etc., should be sub-divided into the most suitable classes, and it will generally be found desirable to write off to revenue the original cost and the additions made each year over a short term of years in equal instalments. As in the case of the more important plant, it will be necessary also to sub-divide the loose plant, etc., departmentally, so that the proper charge for depreciation may be determined for each department of the works.

Furniture, Fixtures and Fittings. It is usual to group under this heading all the furniture, fixtures and fittings of a works which are not directly connected with manufacturing processes and included under plant. A Furniture, Fixtures and Fittings Account is also customary in the case of concerns where no manufacturing is undertaken. The rate commonly adopted is 10 per cent., but this may be inadequate when a large proportion of fittings is included in the account, and particularly so when structural alterations of the offices or works are frequently made. In many offices typewriters, adding, and calculating machines form a important section of the Furniture, Fixtures, and Fittings Account. In such cases a separate account should be opened for office machines, and a rate of at least 15 per cent. should be adopted.

Patents, Trade Marks, etc. It is impossible to lay down any rule for the depreciation, if any, of these assets, which are closely allied to goodwill. It may, however, be definitely stated that they suffer no loss through use, and that the question of depreciation is a matter of prudent finance.

As a rule the amounts set aside as reserves for depreciation are, as the phrase goes, "invested in the business," and used as working capital free of interest. If working capital be required there can be no objection to this course, which is simpler and more economical than borrowing for the purposes of working capital, probably at a higher rate than the reserves for depreciation would earn if funded and invested. If, however, the reserves be invested at interest, the rates of depreciation would obviously have to be varied accordingly.

Where it is anticipated that a considerable sum will have to be found in cash at the end of a term of years—for example, to meet the fine upon renewal of a lease—it is very usual to take out a leasehold redemption policy for the amount required at the end of the term. The annual premiums accumulate in the hands of the insurance

company at compound interest, and therefore the surrender value of the policy soon amounts to more than the total of the premiums paid. If the premiums are simply written off to Revenue Account each year a secret reserve is created equivalent to the premiums and the compound interest thereon. The more correct method is to charge the premiums (which are equal to the total depreciation) to Revenue Account, and then by means of cross entries to create a nominal asset equal to the amount of the premiums, plus compound interest, on the creditor side of the Balance Sheet and a reserve on the debtor side of an equivalent amount.

At the end of the term of insurance the insured receives the whole sum insured in cash, out of which he pays the fine upon renewal. By the usual process of accounting, the sum received will extinguish the nominal asset representing the premiums paid and interest, and the amount paid as fine will extinguish the reserve fund, thus closing these two accounts. If, however, the policy is taken up only to recoup over a term of years, a sum paid at the commencement of the term for, say, leaseholds, and there is no further fine or other sum payable, then at the close of the term the nominal asset is extinguished as before by the receipt of the cash, but the Reserve Account is applied to writing off the sum originally paid for the lease. The cash itself remains in the hands of the insured, and is in substitution for the capital originally paid out for the leaseholds. As the sum has been accumulating out of, and charged to profits, in order to recoup a previous capital outlay, it may sometimes prove a nice question to determine how it should be dealt with, whether as capital or as income. This will be governed, in the case of limited companies, by the Articles of Association, and in the case of partners by the Partnership Deed. In the case of a sole trader the question will not arise. (See also REPAIRS AND RENEWALS.)

RENT ROLL.

A list of rents receivable, giving particulars of the property out of which they arise, name of the tenant, and periodical amount. Columns are usually inserted showing arrears of rents brought forward, allowances made to tenants, the net amount due, and the arrears of rent to carry forward to the succeeding rent roll.

RENTES.

The French equivalent for British Consols; that is, Rentes represent the French National Debt, though perhaps it would be more correct to say that the word is properly applied to the interest paid by the Government rather than to the debt itself.

RENTS.

Rents, payable form a charge against revenue. Being of an accruing nature, they are apportionable in respect of time, and the auditor should see that any rent accrued or paid in advance at balancing periods is properly provided for in the balance sheet, so that an equitable charge is made against the Profit and Loss Account. The auditor should refer to the lease or tenancy agreement to determine the amount of the charge for rent and the due date of it.

Where a considerable number of rents receivable exists, as in the case of cottage rents, a rent-roll should be in existence, and the auditor should examine it to see that the rents are regularly received and debited in the Cash Book. Where tenancy agreements exist, they should be referred to and compared with the rents shown as due in the rent-roll. When rents which have been previously received cease to be charged, the auditor should require an explanation, and satisfy himself by reference to any expired agreements which may be produced that the omission is in order. Particular attention must be paid to "empties" and "vacancies," which should be approved by a responsible official.

All rents accrued and all arrears other than those which it is anticipated will not be recovered, should be brought into the Balance Sheet as assets.

In the case of large arrears of cottage rents, it is sometimes advisable to call for the production of the tenants' rent books, but care should be taken that the rent books produced are not fictitious ones prepared for the occasion. (See also AUDITING, p. 80; BANKRUPTCY ACCOUNTS, p. 167; PROFIT AND LOSS ACCOUNT, pp. 788 and 790).

RENTS RECEIVED FROM PREMISES SUB-LET.

It is advisable, where only a portion of the business premises is occupied, and the remainder is sub-let, to debit the Rent Account with the total rent payable and to credit the same account with rents received from sub-letting. In the Profit and Loss Account the gross rent paid should be shown, with the rents received from sub-lessees appearing as a deduction, the net rent being carried out. This discloses the facts of the cases, and in the event of the premises sub-let being vacant and causing the full rent to be charged against Profit and Loss, the fluctuation is self-explained.

The tenancy agreements with the sub-lessees should be produced to the auditor in verification of the sums received from this source, and accruing rents or rents paid in advance should be properly apportioned and carried into the balance sheet as assets or liabilities respectively. Vacancies during which no rent is received should be approved by

an official in authority, and the approval should be produced to the auditor in support of the omission to record the rents which otherwise would be receivable.

REORGANISATION AND REDUCTION OF CAPITAL.

(See LIMITED COMPANY ACCOUNTS, p. 636.)

REPAIRS AND RENEWALS.

Repairs, being the cost of maintaining the earning capacity of capital assets, should be charged against revenue. This also applies to renewals, when those renewals are merely heavy repairs. But where an absolutely new machine is installed to replace a worn-out or obsolete old one, the cost of this renewal may be debited to Plant Account, provided the cost of the old machine has been reduced (by writing off depreciation) to its scrap value. In certain cases where exceptional repairs have been undertaken, it is permissible to spread the cost over a short period, inasmuch as the benefit to be derived from the repair will probably be felt for some time after the actual period, within which the expense was incurred, has ended.

Care should be taken by the auditor that all repairs are properly charged to revenue, and, in cases in which renewals are debited to the Capital Account, that the asset which is replaced has been properly written off, otherwise it means an over-valuation of the asset in the balance sheet. In many classes of business the expenditure upon repairs bears a fairly constant ratio to the turnover, or to the number of machines, and a comparison of this ratio with that of previous periods, and with those in the accounts of similar businesses, will form a good test for the auditor to apply in checking the adequacy or otherwise of the sum charged for repairs. (See also DOUBLE ACCOUNT SYSTEM, p. 424; PROFIT AND LOSS ACCOUNT, p. 791.)

REPAIRS EQUALISATION FUND.

The object of the creation of a Repairs Equalisation Fund is to equalise the charges for repairs against succeeding periods. The contributions to the fund, which should be charged against Profit and Loss Account, should be determined by an examination of the experience of the cost of repairs over a fairly long period. The contributions are regularly credited to the fund, and the actual repairs executed during any period are debited to the fund. As a consequence, the balance on the fund at the close of each period should be a credit balance. If the balance be a debit balance, then, unless it is caused by some exceptionally heavy repairs being executed, such

as may be due to a breakdown in the machinery, it is obvious that the contributions to the fund, and consequently the charges against revenue, are insufficient, and the auditor should require them to be increased. A temporary overdraft on the fund, due to some such circumstance as that mentioned above, may, however, be permitted.

REPLACEMENTS.

(See DOUBLE ACCOUNT SYSTEM, p. 425.)

REPLEVIN.

(See DISTRESS.)

REPUTED OWNERSHIP.

Sometimes a person is so placed with regard to certain goods and chattels that he appears, to the outside world, to be the owner of the same, although, as a fact, they are not his property. Upon this assumed ownership other persons are often induced to give credit and finally to sustain losses. This is provided against by the Bankruptcy Act, which sets out that amongst the property which is divisible amongst the creditors of a bankrupt are to be included "all goods being, at the commencement of the bankruptcy, in the possession, order, or disposition of the bankrupt, in his trade or business, by the consent and permission of the true owner, under such circumstances that he is the reputed owner thereof." The question whether a trader has allowed his goods to be in the possession and at the disposition of the debtor under such circumstances is entirely a question of fact.

REQUISITIONS OF TITLE.

These are certain questions which are put forward by the proposed purchaser of an estate to the vendor of the same, when a contract for the sale of real estate is being negotiated between the parties. If the contract has been properly framed, these requisitions are most important since they are generally made the foundation of the special terms of the contract.

RESERVE ACCOUNT.

An account kept for the purpose of setting aside profits which it is not desirable to distribute as dividends, and which may afterwards be utilised for the purpose of meeting extraordinary losses, or to equalise dividends in years showing poor results.

RESERVE AGAINST DEPRECIATION OF SECURITIES

(See PROFIT AND LOSS ACCOUNT, p. 792.)

RESERVE CAPITAL.

By Section 59 of the Companies (Consolidation) Act, 1908, a limited company may, by special resolution, determine that any portion of its share

capital which has not been already called up shall not be called up unless for the purpose of winding up. Capital so treated is known as 'Reserve Capital.'

RESERVE FOR BAD DEBTS.

(See BAD AND DOUBTFUL DEBTS RESERVE; BALANCE SHEET, p. 142.)

RESERVE FOR CLAIMS UNDER POLICIES.

(See BALANCE SHEET, p. 142.)

RESERVE FOR DISCOUNT.

(See DISCOUNT, RESERVE FOR.)

RESERVE FOR EXPECTED GAINS.

(See ADJUSTMENTS AT BALANCING TIME.)

RESERVE FOR EXPECTED LOSSES.

(See ADJUSTMENTS AT BALANCING TIME.)

RESERVE FUNDS, INVESTMENT OF.

The problem of investment of reserve funds has received in the past a large share of the attention of the leading accountants.

An examination of the authorities reveals a wide difference of opinion. One tells us that "a reserve fund is not merely a surplus shown on the debit side of the balance sheet, but must be represented by special investments." On the contrary, another is of the opinion that the term "Reserve Fund" is properly used for the surplus, whether invested or not; whereas such a surplus has been described as a "reserve" or "rest."

The main difference of opinion appears to be one of terminology, which is, of course, largely a question of individual taste. The more important question is whether the surplus or reserve fund should be invested; and in determining this, we must inquire into—

- (1) the objects of the fund;
- (2) the advisability of investment in each particular case.

In addition, we must consider whether the existence of the reserve fund is dependent on or assured by the investment.

Dealing with the objects of a "Reserve Fund," they may be some or any of the following—

- (1) to equalise dividends;
- (2) to take advantage of good years to tide over less successful periods;
- (3) to provide for unknown contingencies;
- (4) to provide working capital by accumulating revenue;
- (5) generally to lend stability to the company.

Taking these various cases, it will be seen that purposes (1), (2), and (3) will be served as well if the funds are available, whether they are in the business or out of it. For purpose (5) it is advisable to invest outside the business, provided a sufficiency of working capital is maintained. For purpose (4) it is essential that the money be in the business, otherwise the objects of the fund will be defeated.

It will be seen that under this heading the balance appears to be slightly against investment where the money can be better employed in the business. Where there is a surplus of cash, it must, of course, be invested; but this, it will be seen, is the result of a surplus of *cash* and not of profits, and might arise even where no reserve fund exists.

Investments outside the business are always an advantage to a business provided the company can afford to invest, and this proviso is the main consideration in the question.

A company should not make such an investment if it would by so doing deprive itself of a sufficiency of working capital; *e.g.* if a company already has a bank overdraft, it would be suicidal further to increase its liability by investing in, say, gilt-edged securities; it would lose 2 or 3 per cent. per annum and receive no advantages to compensate the loss.

Again, where a company can more advantageously employ its funds in or about its own business it would be, as a general rule, bad policy to invest elsewhere; *e.g.* if a company owns its business premises, which are mortgaged at, say, 4 per cent., paying off the mortgage would be a better "investment" than, say, Consols; but it should be noted that in this case provision must be made for all contingencies that may be reasonably expected.

These considerations will not apply where the reserve is raised for a specific purpose; *e.g.* a sinking fund raised to repay a loan or issue of debentures, or to provide for the renewal of a wasting asset. In this case the nature of the fund demands that actual cash shall be available at a certain date, hence the necessity for the investment; but this is not, strictly speaking, a reserve fund.

The following example is of interest in connection with this subject. Assume that a company has the following balance sheet—

BALANCE SHEET (No. 1)

Capital (paid up) \pounds 100,000	Sundry Assets . \pounds 90,000
Reserve Fund 10,000	Another Asset . 10,000
	Reserve Fund
	Investment . 10,000
<u>\pounds 110,000</u>	<u>\pounds 110,000</u>

Now assume that the asset, \pounds 10,000, is totally lost. The balance sheet would now appear—

BALANCE SHEET (No. 2)

Capital (paid up) \pounds 100,000	Sundry Assets . \pounds 90,000
	Reserve Fund
	Investment . 10,000
<u>\pounds 100,000</u>	<u>\pounds 100,000</u>

Again, assume that the investment is sold at the stated value and the proceeds used in the business. Balance Sheet No. 1 would now stand amended as follows—

BALANCE SHEET (No. 3)

Capital (paid up) \pounds 100,000	Sundry Assets . \pounds 100,000
	(90,000 + 10,000)
Reserve Fund . 10,000	Another Asset . 10,000
<u>\pounds 110,000</u>	<u>\pounds 110,000</u>

The example reveals these facts—

(1) Balance Sheet No. 2 shows that the reserve fund can be absorbed and the investment remain; hence the existence of the fund is not assured by the investment;

(2) Balance Sheet No. 3 shows that the investment can be sold and the reserve fund remain; hence the existence of the fund is not dependent on the investment; thus leading us to the conclusion that a reserve fund is no less a reserve fund even if not invested.

Investment outside the business undoubtedly has the effect of strengthening the concern, and the advocates of the investment of reserve funds have this important factor in their favour. The respective opportunities of making the investment and raising the fund are frequently coincident, but merely because of these facts we cannot lay down the rule that a reserve fund must or ought to be invested, since it has been shown that the fund is no more secure merely because there is an outside investment among the assets, that the investment of moneys has no connection with the fund raised out of profits, and that there are a great number of very obvious cases where it ought not to be invested.

The question of investment should be decided by weighing the added stability resultant on investment against expediency or advisability in each particular case along lines above indicated. For the rest, if the surplus is invested, we may without fear call it a "Reserve Fund"; but if it is not, then all shades of opinion will agree to call it a "reserve," a "rest," or "reserve account"; but, however we label it, we must remember it is always substantially the same thing. (See also RESERVES AND RESERVE FUNDS.)

RESERVES AND RESERVE FUNDS.

RESERVES.—The word "Reserve" is used to describe a variety of items in the Balance Sheets of profit-seeking undertakings, for it has a wide range of meaning and is indiscriminately applied to conditions which are often even conflicting and in opposition to one another. The word is thus unsuitable for general use in connection with the accounts of profit-seeking undertakings because its wide range of meaning and consequent lack of accurate definition gives rise to much confusion of thought. In considering the subject, therefore, it will first be necessary to set out the nature of the varying conditions referred to and to apply individual definitions to these. For the sake of clearness, these definitions will be used in this article in place of, or sometimes in company with, the word "Reserve."

It will be seen, therefore, that under the present practice it is impossible to know the true meaning of the word "Reserve" in the Balance Sheets of profit-seeking undertakings, and that the word is unsatisfying and is not suitable for use in financial accounts. It will be granted that the operation which purports to provide a charge against revenue of a kind necessary before there can be any true profit is conflicting and in opposition to the operation which purports to represent the retention in hand of true profit, and yet the word "Reserve" is applied equally to both, and no doubt in its dictionary meaning it is equally applicable to both, as will be seen by reference to the following extracts from the New English Dictionary—

RESERVE SB.

"Something stored up, kept back, or relied upon for future use or advantage."

1868. Rogers Pol. Econ. IX (1876) 103. It is a maxim in business that a man . . . should have a hoard or reserve from which he can draw, when the times are untoward.

"The amount of capital kept on hand by a banker, insurance company, etc., in order to meet ordinary or probable demands."

1885. Jnl. Inst. Actuaries. Apr. 141. On a new method of comparing the Reserve for Policies.

RESERVE V.

"To keep for future use or enjoyment; to store up for (to) some time or occasion; to refrain from using or enjoying at once."

To keep (a matter) from the knowledge of others. 1719. De Foe Crusoe 11 (Globe) 322. The ideas of Things which we form in our minds perfectly reserved, and not communicated to any.

A study of these extracts shows clearly that the word "Reserve" is, accurately applied to

anything stored up or kept back for future use, and, in financial accounts, this may be either a provision to answer now existing liabilities of uncertain amount, or to provide for the replacement of that part of the capital outlay which, to an uncertain extent, has already expired, or when it concerns profit it may be a retention of profit in hand to be available for future distribution. Any amount of profit so available for future distribution is, as stated above, better described as surplus than as reserve.

RESERVE FUNDS.—Whenever a true surplus exists, there is an equivalent amount in the hands of the undertaking, which, if absorbed in the business of the undertaking, forms an internal surplus or reserve; and if invested in other forms of value outside the actual business of the undertaking, constitutes what is known as a Reserve Fund. As the word "Reserve" is, for the reasons given, unsuitable for use in financial accounts, so, in the same way, the term "Reserve Fund" as at present used is too indefinite and has too wide a range of meaning for practical purposes in connection with the accounts of profit-seeking undertakings. Thus, amongst the meanings given to the word "Fund" in the New English Dictionary are the following—

FUND. SB.

"A stock or sum of money, esp. one set apart for a particular purpose."

1868. G. Duff Pol. Surv. 25. There is a 'reserve fund, valued at from two to three times the amount of the yearly expenditure.

"A portion of revenue set apart as a security for specific payments."

FUND. V.

"Originally to provide a 'fund' for the regular payment of the interest on an amount of public debt, hence to convert a floating debt into a more or less permanent debt at a fixed rate of interest."

At present the word "Reserve" is applied to items representing sums kept back out of revenue receipts—by being charged to Revenue Account—either for the purpose of meeting, at a future time, some otherwise unprovided for liability which has accrued and is chargeable against revenue receipts, or for the purpose of making provision for ultimate replacement of that part of the capital outlay which has already expired in the process of seeking profits—both being part of the cost of seeking profits. In either case, the word "Provision" serves better than the word "Reserve" to distinguish the object and effect sought to be attained, as the provision out of revenue is necessary before the balance of the Revenue Account can represent true profit.

And the word "Reserve" is also applied to items representing sums of true profit retained in

hand for future use, and in this case the meaning is better distinguished by using the word "Surplus," for there should be surplus value to a corresponding amount existing in the hands of the undertaking. The surplus may be either an internal surplus, as when the sums retained in hand are invested in the business of the undertaking, or it may be an external surplus, as when they are invested in securities or other forms of property in the hands of, but outside the actual business of, the undertaking when the term Reserve Fund is properly applied. It is because the word "Reserve" is at present indiscriminately applied to items which may be either a necessary provision of amounts before profit can be ascertained, or a surplus consisting of true profit retained in hand, that so much controversy has arisen, the confusion being increased owing to the fact that these so-called reserves often include, in one item, both provision and surplus in unknown proportions.

In present accounting practice the terms "Reserve" and "Reserve Fund" appear to be indifferently applied to describe items of the same character, so that in the case of one undertaking the word "Reserve" will appear in the Balance Sheet against a particular kind of item, while, in the Balance Sheet of another undertaking, it will be described as "Reserve Fund." A discussion of the meaning of the word "Fund" in financial accounts leads into difficult and debatable ground. In financial accounts the word "Fund" seems to have at least two distinct and altogether different meanings. The first meaning is identical with the meaning of the word "Surplus" as explained above, and there can be no true surplus unless there exists in the undertaking an excess of assets over the sum of liabilities and subscribed capital. The other use of the word "Fund" has a different meaning, and is the popular way of alluding to the amount of an investment set aside for a particular purpose. Unless there is a true surplus the word "Fund" used in this sense can only indicate a particular investment or asset, and the existence of this investment or asset is no proof that there is any surplus or true fund in the hands of the undertaking, for the word "Fund," in its dictionary meaning, may be used to indicate a valuable asset of any kind.

Confusion Between "Provisions" and "Surpluses." In the Balance Sheets of many undertakings large sums appear as reserves, representing both provisions and surpluses of one kind or another, and there is a tendency to confuse the "provisions" with the "surpluses." This is unfortunate because the provisions represent actual loss or expired capital outlay, whereas the surpluses represent profit retained in hand. It seems at first sight to be inexplicable that the word "reserve" should be used to represent losses and expired capital outlay as well as profit retained

in hand. But the reason of this apparent contradiction is that, in order to arrive at true profit, it is necessary to deduct from the revenue receipts of the year not only the current expenses of the year which are payable in cash, but also to deduct expired capital outlay on industrial plant and other wasting assets used by the undertaking in earning the revenue. This latter class of expense is, however, often to a large extent ignored in preparing the Revenue Account, the effect being to cause the credit balance of the Revenue Account to represent more than the true profit, and to leave the book value of the plant and other wasting assets at a higher figure than the true value.

But in these circumstances, as a precautionary measure to guard against the distribution of too large a dividend, a portion of the credit balance of Revenue Account is often transferred to a "Reserve" Account, without attempting systematically to ascertain and provide for that part of the expense connected with revenue earning which is represented by expired capital outlay on wasting assets. Thus, a covering sum is transferred from Revenue Account in the hope that the amount is on the safe side, and that it will enable those responsible for the management of the undertaking to meet any contingencies which may arise in the future. Assuming that the amount so set aside is a liberal one, and is more than the true amount of expired capital outlay representing part of the expense of earning the year's revenue, it will consist partly of loss or expired capital outlay and partly of true profit, which will remain in hand undistributed owing to its having been so transferred from Revenue Account to the credit of a Reserve Account. It is probable that, in the near future, unexpired capital outlay will by common consent have to be accounted for systematically and on a settled and recorded basis year by year as it expires, thus enabling the true profit or loss of each year to be more accurately ascertained, and "provisions" clearly distinguished from "surpluses."

Provisions made against Assets should be Deducted from Assets. In all profit-seeking undertakings it is necessary to prepare a periodical statement, usually an annual statement, in the form of a Balance Sheet purporting to show on one side the best possible estimates of the fair "going concern" values of the assets in the hands of the undertaking at the date of the Balance Sheet, and, on the other side, the full debts owing by the undertaking at the same date. The surplus of the assets over the debts owing by the undertaking should show the capital invested in the undertaking, but it sometimes happens that the book values—that is, the Balance Sheet values—of the assets are allowed to remain at sums greater than the fair "going concern" values at the date

of the Balance Sheet, and, as a set off against this, provisions, called reserves, have been raised in the books by means of the gradual accumulation of amounts charged against the revenue receipts of former years before the balance of profit was struck. Sums accumulated in this way may be set out in a Balance Sheet on the liabilities side, but they are better dealt with by being deducted from the appropriate items on the assets side of the Balance Sheet, and, as already explained, in either case they represent that form of reserve which is better described by the word "Provision," because it does not in any sense represent a surplus.

Different Classes of "Provisions." This form of so-called reserve representing a provision may be divided into three classes—

(1) To cover estimated expired capital outlay on wasting assets.

(2) To cover estimated losses incurred on capital invested in stock-in-trade, book debts due to the undertaking, securities and shares in outside undertakings, and in all kinds of property other than wasting assets.

(3) To cover estimated liabilities accrued over and above the regularly recorded debts owing by the undertaking.

Classes 1 and 2 are easily distinguishable in character from Class 3, in that they stand for losses of capital outlay and purport to represent the best available estimates of actual expense or loss incurred under this head but not otherwise recorded in the books, whereas Class 3 represents an estimate of otherwise unrecorded liabilities.

It will be noticed that all provisions apply to something which must be estimated because it is uncertain; thus, the first class relates to expired capital outlay on wasting assets, which is a very important factor in the cost of seeking profits, but it must be estimated. This subject is dealt with more fully in the article on Depreciation. It is, doubtless, owing to this element of uncertainty that these provisions have come to be known as reserves, that is to say, a portion of revenue reserved to answer an expense which is of uncertain dimensions but which is incidental to the earning of revenue. Other expenses incidental to the earning of revenue, such as wages, salaries, rent and the like, involving the payment of cash in or about the period when the consideration is consumed in the earning of revenue, are easily measurable, and can be ascertained year by year with precision, but the expired capital outlay on wasting assets cannot be so ascertained, although it is nothing more than long period revenue outlay, being incurred solely in order to earn the annual revenue over a series of years during which the value will expire, except as to any scrap or remainder value.

The second class comprises provisions for losses

incurred which are also incidental to the earning of the revenue and which must be estimated. Such losses may be represented by the fall in value of stock-in-trade while it is held for sale, due either to market movements in price or to physical deterioration from any cause, or they may be represented by book debts turning out to be bad debts, or by a fall in the market value of investments in outside securities or ventures of any kind belonging to the undertaking. Provision for losses on money invested in outside securities can only be said to be incidental to the earning of the revenue of the undertaking, if and so far as the nature of the business needs the use of a fluctuating amount of money, thus creating the necessity of holding temporary investments.

These provisions for estimated expired capital outlay and for probable estimated losses incurred on capital invested in stock-in-trade, book debts, etc., are, as already stated, often shown on the Balance Sheet of a profit-seeking undertaking on the liabilities side under the name of reserves, leaving the assets, in respect of which these provisions are made to appear among the assets on the other side of the Balance Sheet at sums larger than their estimated going-concern values. This is, as a rule, open to the objection that such values, according to the best available estimates, are then overstated on the assets of the Balance Sheet. It is clearer to state the assets in the Balance Sheet at the net amounts representing their going-concern values. Another plan sometimes adopted is to show on the Balance Sheet the amount representing the original cost of each asset, and then to show as a deduction in each case the provision which has been made in respect of expired capital outlay, or for probable losses on other assets, carrying out in each case the net amount representing the estimated actual value. This plan is also apt to be confusing, being open to the objection in the case of capital outlay on wasting assets, that the sum of the cost continues to accumulate year by year, as also does the sum of the annual provision, so that, in course of time, both these accumulating amounts become meaningless, because they include expenditure in past years which may have wholly expired and been replaced over and over again by new wasting assets.

If the assets are shown in the Balance Sheet at their going-concern values, that is to say, after deducting all provisions needed to meet estimated losses in connection with the assets, and if the liabilities are fully stated as liabilities, then all reserves appearing as such on the liabilities side of a Balance Sheet must be in the nature of surpluses representing previously earned profits remaining undistributed, or profits accruing to the undertaking from a special source—as, for instance, the issue of shares in the capital of the company at a premium—and the common adoption

of this plan would make the true nature of reserves—as surpluses—more clearly apparent and would tend to avoid the misconception which at present so commonly exists.

Illustration of Provisions and Surpluses. In order to make clearer the meaning of provisions and surpluses—commonly called reserves or reserve funds—it is desirable to set out a *pro forma* Balance Sheet containing two columns A and B, and Profit and Loss Account in which

provisions and surpluses are shown under a number of different heads, as below.

It will be noticed that the figures in the Balance Sheet are stated in two ways, in parallel columns lettered A and B. The figures in Column A show the method which is sometimes adopted of stating the provisions as well as the surpluses on the liabilities side. As already stated, the provisions differ from the surpluses to the extent that the former really represent expenditure actually

PRO FORMA BALANCE SHEET, 31ST DECEMBER, 19..

[illegible]

PRO FORMA TRADING AND PROFIT AND LOSS ACCOUNT FOR THE YEAR ENDED 31ST DECEMBER, 19..

	£	s.	d.	£	s.	d.		£	s.	d.
Stock at beginning of year				35,000	0	0	Sales	122,500	0	0
Purchases				30,000	0	0	Stock at end of year	37,500	0	0
Wages				50,000	0	0				
Trade expenses				17,200	0	0				
Expired capital outlay (estimated) —										
Buildings on Freehold Land	250	0	0							
Leaseholds	50	0	0							
Plant and Machinery	1,500	0	0							
				1,800	0	0				
Estimated loss on realisation of										
Stock				1,000	0	0				
Balance being Gross Profit				25,000	0	0				
				£160,000	0	0		£160,000	0	0
Selling, management, and office expenses				10,400	0	0	Balance down	25,000	0	0
Bad Debts, including £100 added to provision				600	0	0				
Interest on Debentures				1,000	0	0				
Balance being net profit as per Balance Sheet				13,000	0	0				
				£25,000	0	0		£25,000	0	0

incurred in the process of profit-seeking, whereas the surpluses should represent true profits which are retained in the business instead of being distributed. Surpluses are often stated in the Balance Sheet under various names as shown in the above *pro formâ* Balance Sheet, the contents of which may now be considered in detail.

The first item appearing on the left-hand side of the *pro formâ* Balance Sheet in which the word provision is used is "Provision for interest accrued £500." This is typical of that class of provision representing any liability which has partly accrued but has not become due at the date of the Balance Sheet, and so has not been carried to the credit of any definite creditor's account in the books. It is a liability in the process of accruing which must be provided for in the accounts although no sum of money has, at the date of the Balance Sheet, become due or payable by the business in respect of it. Provisions of this character, therefore, represent part of sums which will ultimately fall to be paid by the business in cash to creditors.

The next class of provisions represents the sum of the annual provisions set aside out of the revenue receipts of each year to make good the expired capital outlay on wasting assets employed by the undertaking in seeking profits. These wasting assets include such property as buildings (excluding freehold land), leaseholds, and all kinds, of plant and machinery. Properly considered all outlay on property of this kind made for the use of an undertaking seeking profits, represents payments made in advance on Revenue Account, the "going concern" or accounting values of

which expire year by year. Such property is not intended for sale, but is intended to be applied to the purpose of seeking profits, and in this process the value will gradually expire, except only as to any scrap value which may remain at the end of the efficient life of each of the various kinds of property.

In industrial and commercial accounting it is necessary always to regard the undertaking as a going concern, in conformity with the object for which the capital outlay on the wasting assets was incurred; and in preparing the annual accounts, therefore, the important question to determine in connection with all wasting assets, is how most equitably to spread the cost, less the estimated scrap value, over the Revenue Accounts of each year during the efficient life of each class of wasting assets. This subject is more fully dealt with in the article on "Depreciation," but the point which must be made clear here is that expired capital outlay on wasting assets, although it can be the subject of estimate only, is a part of the cost of seeking profits equal in importance to other revenue expenditure.

Taking this class of provisions as shown in the *pro formâ* Balance Sheet item by item, the first relates to buildings on freehold land, and amounts to £2,250 in respect of buildings which cost £10,000. This would obviously be best dealt with by being deducted from the item on the right-hand side of the Balance Sheet representing the value of freehold land and buildings, because, assuming the rate of deduction has been settled with reasonable care and the provision duly made year by year, the present value of the buildings is

nearer to £7,750 than to £10,000, and the same observation applies to the next item, leaseholds, in which case it is equally misleading to show the value of the leaseholds at £1,000 among the assets, when it is probable that the value is nearer to £750.

In the case of provisions for estimated "expired capital outlay" on plant and machinery, which is commonly called "depreciation," the case becomes still clearer in favour of showing the asset under this head at its net estimated value. In Column A the value of the plant and machinery appears to be £30,000, but on the other side, under the head of provisions, is an amount of £13,500, which includes £1,500 charged to the Profit and Loss Account of the year ending at the date of the Balance Sheet. It is probable that the £30,000 assumed to be the cost of plant includes the cost of many items which have, during the time the business has been carried on, become worn out and been discarded. Assuming that sufficient depreciation has been provided year by year, the full cost, less the scrap value of all such discarded plant, has been provided and is included in the £13,500 appearing under the head of provisions, and this method (which operates to accumulate mere outlay not represented by value on one side of the Balance Sheet and provisions against that part of the outlay which has expired on the other side of the Balance Sheet) is obviously undesirable because the figures taken separately are meaningless. For this reason, provisions for estimated expired capital outlay on wasting assets should be deducted from the cost of the wasting assets in respect of which the provisions are made, so that these values will appear net on the assets side of the Balance Sheet, that is to say, at the amounts which most nearly approximate to their true values to the undertaking as a going concern.

The next class of provisions is for estimated loss on realisation of other assets, and as the assets shown on the Balance Sheet are necessarily held for the purposes of the undertaking, any loss in realising them must be provided for as a charge against the Profit and Loss Account before the balance of net profit is struck. Although the stock of raw and partly manufactured material, and the manufactured stock may be valued on a normal and proper basis, the directors, in consultation with the management, may feel that it is desirable, for some good reason, to make a provision against loss on realising some of this stock, in which case it is to be assumed that, according to the best opinion, it is probable that a loss will be sustained. The amount can only be estimated, but it is obvious that the net profit is more likely to be stated with approximate accuracy after a provision of this character has been made than if the question is ignored. Such provisions should be deducted from the amount

at which the stock is entered in Column A in the Balance Sheet, instead of being shown as provisions on the liabilities side.

The provision for bad debts is a necessity common to most undertakings and is generally deducted from the amount at which the debtors appear on the assets side of the Balance Sheet, and not as shown in Column A. Where there are outside investments, provision for any probable loss on these must also be charged against the Profit and Loss Account, assuming that such investments have been made for the purposes of the business instead of depositing at the bank moneys not required for present use, at a rate of interest lower than that yielded by the outside investments.

The provision for estimated expired capital outlay on goodwill and patent rights is the next item which appears on the left-hand side of the *pro forma* Balance Sheet. The need of making a regular provision for expired capital outlay on goodwill, patent rights and copyrights is still a vexed question, and widely different opinions are held on the subject. The matter is discussed at length in the article on "Goodwill." When provision is made in respect of this item it is clearly an allocation of part of the profits earned, and it will be seen on reference to the article on "Goodwill" that the annual provision represents a share of the profit of the particular year, bought in advance of its arising, and paid for in the price paid for the goodwill. This being so, the provision for estimated expired capital outlay on goodwill and patent rights represents only the gradual refunding of the amount paid for purchased goodwill as the value comes back, and, therefore, the amount should not be shown on the left-hand side of the Balance Sheet, but should be deducted from the gradually expiring cost of the purchased goodwill and patent rights included amongst the assets on the Balance Sheet.

A consideration of what has been said above will show that the provisions appearing in Column A on the left-hand side of the *pro forma* Balance Sheet should not be shown there at all. These amounts are lined round in the Balance Sheet. It will be seen that the provisions have been added to, during the year covered by the Profit and Loss Account annexed to the Balance Sheet, to the extent of £2,900, being the sum of several items charged against the year's revenue, and to the extent of £3,000, the amount allocated out of the year's profits for expired capital outlay on goodwill.

What becomes of the Money Representing Provisions and Surpluses? It is often difficult to understand what becomes of the money taken out of revenue in respect of the various provisions and surpluses. This money will not usually be found accumulating at the bank, and therefore,

to the uninitiated it appears as though these transfers do not really result in providing money for the several purposes intended. This is a misapprehension, however, for the setting aside of these sums always involves the retention of moneys, because the amounts are charged to, and thus reduce, the credit balance of the Revenue Account. It is the credit balance of the Revenue Account which is distributable as being the profit, and the mere fact of charging amounts to the Revenue Account, therefore, causes a portion of the revenue receipts to be retained in hand by reducing the balance of profit shown on the Revenue Account. This so reduced balance is true profit, being the proportion of the revenue receipts left over after providing for current expenses payable in cash out of the revenue receipts day by day, as well as for expired capital outlay, which, having been previously paid out of capital, must be retained out of revenue receipts each year, and so gradually refunded as the capital outlay expires in the process of profit-seeking—that is to say, as the value disappears.

If these provisions had not been charged against revenue, it is obvious that the balance of Revenue Account shown as distributable profit would have been larger, and that the cash required to be paid away as dividends would be greater, and thus the charging of these sums to revenue has operated to cause a less sum to be drawn from the bank for the dividends. As this process goes on year by year it would seem reasonable to expect that the amount at the bank should gradually accumulate, so that when the particular wasting assets required renewing and the other anticipated contingencies arose, the money retained for those specific purposes would be found at the bank. But, in the meantime, other needs have arisen for the use of more money, either for renewing other plant or for extending the plant, or perhaps the business has increased to an extent needing the purchase of a larger amount of stock-in-trade, or the giving of more credit to customers; all of which conditions would cause more and more money to be imperceptibly absorbed out of any available balance at the bank. The same thing happens to surpluses accumulated out of profits retained in hand for any purpose instead of being distributed, and to sums received in the form of premiums on issues of shares when the premiums are not distributed as dividends to shareholders.

Surpluses may be Capitalised. Reserves, when they represent surpluses, may be capitalised. Thus, a company with a capital of £50,000, consisting of 50,000 shares of £1 each fully paid, and having reserves under one or more heads appearing on the Balance Sheet at £50,000 may capitalise these reserves by issuing to its shareholders one further share of £1 each fully paid in respect of each share at present held, and the legal formalities

having been complied with, the capital will thereafter appear on the Balance Sheet as £100,000, consisting of 100,000 shares of £1 fully paid. But capitalisation of the reserves makes no difference to the intrinsic value of the shareholders' holdings. The profits earned by the company with the help of the reserves (surpluses) are not altered by the process of turning these reserves into an equivalent amount of fully-paid shares. The shareholders have more shares but not more profits. There is a greater number of shares over which to distribute the same profits, and if the market value of the shares prior to the capitalisation of the reserves was £2 each, it will, after the issue of the new shares to cover the reserves, be £1 only. In the case of undertakings such as bank and insurance companies, where there is a large uncalled liability on the existing shares, it is probable that the operation of capitalising any part of the reserves by applying this, not to the issue of new shares, but to the payment off of part of the existing liability for future calls, would have the effect of increasing the market value of the shares to a greater extent than the amount of uncalled liability cancelled, the reason being that partly paid shares are disliked by many investors, and are, therefore, in comparatively small demand.

Secret Reserves (Surpluses). Secret reserves often exist, especially in banking and other undertakings in connection with which a reputation for invincible financial strength is of paramount importance. A secret reserve in the nature of a surplus may be accumulated in various ways, as, for instance, by making unreasonably large provision for losses on book debts or for expired capital outlay on any class of wasting assets. Again, lands or investments in securities and other interests which have largely increased in value may be stated in the balance sheet at cost price. Occasionally valuable property is altogether omitted from a balance sheet, as in the case of the Bank of England, in the accounts of which the value of the premises in Threadneedle Street is omitted. In such cases a secret reserve exists.

The usual and only defensible object of a secret reserve is to have a surplus available in time of stress, which will be available as a set off against heavy and unexpected losses. But the practice may lend itself to abuse in the hands of unscrupulous individuals, who, by excessive provisions, can accumulate secret reserves without the shareholders knowing the true position. Consequently, it is possible that needlessly small dividends may be paid on the shares, which may consequently be offered on the market at a sum less than their true value and be bought up quietly by those who happen to know the true position of affairs.

In an important case before Lord Justice Buckley, it transpired that the Birmingham Small

Arms Company had passed special resolutions empowering the directors to create, but not to disclose, a secret reserve. The facts were, however, to be disclosed to the auditor, but he was not at liberty to state them to the shareholders. The Court observed that the purpose of a Balance Sheet is "primarily to show that the financial position of the company is at least as good as there stated, not to show that it is not or may not be better. The provision as to not disclosing the secret reserve in the Balance Sheet is not necessarily fatal to the special resolution." But the provision as to non-disclosure by the auditor was fatal, so the Court held, because inconsistent with the statutory duty of an auditor. (See also *AUDITING*, p. 90; *BALANCE SHEET*, pp. 141, 142.)

RESERVES, CAPITALISATION OF.

At the close of the year a private trader credits his profits less his drawings or debits his losses plus his drawings to his Capital Account. By a simple process of book-keeping he capitalises his profits or losses from year to year. If he does not require the whole of the capital in his business he may withdraw it and invest it in securities.

An incorporated company cannot so simply increase or decrease capital. It may divide the whole of its profits or carry part or the whole to a reserve or carry forward a loss. The share capital remains nominally as it was and can only be increased or decreased in accordance with the regulations laid down by its constitution or enacted by law. If it is a Parliamentary company, its proceedings are governed by Act of Parliament; if registered under the Companies Acts by its Memorandum and Articles of Association.

The Act or the Articles usually provide that before paying any dividends the directors may carry such sums to reserve as they think fit. Otherwise the whole of the profits would be divisible according to the rights of the respective shareholders. It is seldom stipulated that the reserves so created shall be invested outside the business of the company, nor, as a rule, could such stipulation be conveniently carried out. The surplus profits out of which reserves are created are seldom available in cash, but are locked up in stock, book debts and such like, the dividend usually absorbing as much cash as can be spared. The reserves are, in fact, being used as working capital just as in the case of the private trader; and if, by a book-keeping entry, the surplus profits could be added to the share capital or the losses deducted from it the analogy would be complete. The underlying principle is the same, but the legal position differs.

A growing business requires a growing capital, and if no reserves were made and the whole of the profits divided, the shareholders would require to subscribe more share capital or the

directors would have to borrow in order to carry on.

The directors could divide the profits by way of dividend and then invite the shareholders to subscribe share capital—to put the dividends in one pocket and find cash for shares from the other. As regards profits accumulated as reserves, this, in fact, was the process followed in the case of the Consett Iron Company which, as regards shares in the company vested in trustees under a will, led to litigation between a life owner and a remainderman in the well-known case *Bouche v. Sproule* (12 App. Cas. 385), in which it was held that the shares were part of the capital of the trust.

If the accumulated income be retained in the company's business as a reserve, a form of capital which does not absorb profits by way of interest, the shareholders ought *prima facie* to get increased dividends on the share capital, which remains the same, and the market value of the shares should increase accordingly. Sometimes the shares go to so high a premium as to make them less marketable. In such cases, at one time, companies used to liquidate and reconstruct with a larger share capital, the shareholders receiving more fully paid shares in the new company than they held in the old without finding more money. Owing to a lack of flexibility in the legal procedure relating to companies this process is not only expensive but inconvenient, for the liquidation must be carried out and the proceedings advertised just as if the company were insolvent.

The modern method is to amend the Articles if necessary by inserting Articles such as the following—

1. The Company in General Meeting may from time to time resolve that it is desirable to capitalise any part of the undivided profits of the Company, whether standing to the credit of the Reserve Fund or Profit and Loss or otherwise, and accordingly that the said part of the undivided profits be set free for distribution free of income tax among the members in accordance with their rights, and that the same be not paid in cash but be applied in payment in full or in part of shares of the Company and that the said shares be distributed among the members in accordance with their rights.

2. When such a Resolution as aforesaid shall have been passed on any occasion the Directors may allot and issue the shares therein referred to, credited as fully or partly paid up as the case may be, to the members according to their rights, with full power to make such provisions for the case of fractions by the issue of fractional certificates or otherwise as they think expedient. Any General Meeting declaring a dividend may direct payment of such dividend wholly

or in part by the distribution of specific assets, and in particular of paid-up shares, debentures, or debenture stock of the Company, or paid-up shares, debentures, or debenture stock of any other company, or in any one or more of such ways, and the Directors shall give effect to such Resolutions. The Company may at any time and from time to time in General Meeting pass a resolution to the effect that it is desirable to capitalise any undivided profits of the Company (including the whole or any part of the undivided profits for the time being standing to the credit of any Reserve Fund, Suspense Account or otherwise, or any profit realised upon the sale, or shown by a revaluation of capital assets), and that the same be set free for distribution among the Shareholders in accordance with their rights in the profits upon the footing that the same be not paid in cash but be applied in paying up an equivalent amount of shares of the Company. Any shares issued in pursuance of the powers of this Article shall be distributed among the Shareholders as aforesaid with full power to the Directors by the issue of fractional certificates or otherwise as they think expedient to make provision for the case of fractions, and the Directors shall give effect to any such resolution accordingly, and any shares allotted pursuant to any such resolution shall be credited as fully paid-up by means of the profits aforesaid. If and whenever necessary the Directors shall cause a proper contract to be filed in pursuance of Section 88 of the Companies (Consolidation) Act, 1908, in respect of shares so allotted, and the Directors may appoint any person on behalf of the holders of the shares of the Company, issued prior to such allotment to enter into such contract with the Company, and any such appointment so made and any contract so entered into shall be as valid and effective as if the same had been made and entered into by such Shareholders personally.

Bonus shares are then allotted in accordance with the Articles, and if thought necessary an agreement is filed between the company and the trustee for the shareholders, though the filing of a deed is probably superfluous where the reserve arises out of divisible profits. By this means the dividends paid become proportionate to the real capital at stake—the original capital plus the accumulation of profits—and the shares become more marketable. Moreover, the working capital is definitely retained in the business and the financial position strengthened. There is one danger, and that is that in the event of a severe fall in values, the reserves having been capitalised are no longer available to write down stocks or provide for exceptional losses under forward contracts. In such a case, owing to the reserve having been crystallised as share capital, a

company may be possessed of large liquid resources, but arising out of subsequent losses may have a debit to Profit and Loss Account. If so, when again making profits it can only pay dividends out of them by ignoring the debit to Profit and Loss Account. According to a judicial pronouncement in *The Ammonia Soda Co., Ltd. v. Chamberlain* [1918], 1 Ch. 266, a payment of this nature is, however, quite legal, though it may give rise to the anomalous position that while the assets representing the bonus shares have quite disappeared, the bonus shares remain and are earning dividends. In cases of undue inflation and where reserves have all been capitalised without leaving any provision at all for deflation this may very well happen.

The underlying principle of the case referred to is not unsound. If it were otherwise, the private trader who has a debit to Profit and Loss Account ought in theory, in order to maintain his capital, to starve until his profits wipe out his losses, an obviously absurd conclusion. Another objection to the capitalisation of reserves is that the increase of share capital renders it more difficult to raise new capital when required as the rate of dividend may be decreased and be more difficult to maintain owing to the increase of capital arising out of the issue of bonus shares. In the case of some companies assets have been written up on a revaluation and the increase carried to reserve and bonus shares distributed thereout. Where this course has been adopted all the shareholders have been made parties to a contract of allotment, so that if in a winding up the assets did not realise the figure to which they had been written up and the shareholders were not paid in full they could not make any claim. This course is not practicable in the case of public companies. Even if it be adopted in the case of a winding up and the creditors not being paid up in full, the shareholders would probably be liable to pay up in full and the directors might be liable as having acted *ultra vires*.

The position of the individual shareholder, where through capitalisation of reserves he receives bonus shares, has led to much litigation. As already mentioned, it has been definitely decided that as between life owner and remainderman the bonus shares are capital and go to the remainderman.

It has also been decided that bonus shares are not income liable to Super-Tax in the hands of the shareholders. On the other hand, the private trader pays Super-Tax on the whole of his profits whether carried to capital or otherwise, a distinction which favours the conversion of private businesses into companies so that in effect the trader, as a limited company, may only pay Super-Tax on his drawings.

The Corporation Profits Tax may, however, be looked upon as a preliminary attempt to apply

Super-Tax to company profits whether divided or reserved.

RESERVES, SECRET.

(See SECRET RESERVES.)

RESERVES TO MEET CLAIMS.

(See AUDITING, p. 89.)

RESIDUARY ACCOUNT.

(See EXECUTORSHIP ACCOUNTS, p. 465.)

RESIDUARY LEGACY.

(See LEGACIES.)

RESIDUARY LEGATEE.

This is the person who is entitled under a will to all that remains of the personal property of the deceased after the various legatees have had their claims satisfied. Unless otherwise provided for, the shares of any legatees who predecease the testator fall into the residue and become the property of the residuary legatee. If there is no residuary legatee named in a will, there is an intestacy as to the residue of the property and the lapsed legacies (if any), and this undisposed-of property is divided according to the Statutes of Distributions.

RESOLUTIONS, LIMITED COMPANY.

The business of company meetings is transacted by means of resolutions. The form of the resolution depends primarily on the particular business and the provisions made by statute, and secondarily upon the Articles and Memorandum of Association. For ordinary business and for any other business of the company not specially provided for in the Articles or the Companies Acts, an ordinary resolution is all that is necessary, that is, a resolution passed by a simple majority of those voting at a regularly constituted meeting of the company.

An *extraordinary* resolution is one which is required for certain purposes in winding up, particularly to commence voluntary winding up when by reason of inability to pay its debts the company is of opinion that it should be wound up. Such a resolution is formally passed by a majority of not less than three-fourths of such members entitled to vote as are present in person or by proxy at a general meeting of which notice specifying the intention to propose a resolution as an extraordinary resolution has been duly given.

A *special* resolution is required in all cases of business involving an alteration of the Articles of Association, and in addition in all cases where this kind of resolution is specified in the Articles. Thus the Articles could provide that all business

at an annual general meeting should be transacted by means of a special resolution, although such course would be unusual. A resolution of this kind is passed in two stages; in its first stage it is exactly like an extraordinary resolution, but is not deemed to be carried until it has been confirmed at a specially convened meeting held not less than fourteen days nor more than one month after the date of the first meeting. In the confirmatory resolution the majority required is a simple majority of those persons present and entitled to vote at the confirmatory meeting. A special resolution would in the notice calling the meeting be referred to as such and the substance of the resolution would form part of the notice. (See also MEETINGS OF LIMITED COMPANIES.)

REST.

This is an item which appears on the liabilities side of the weekly return of the Bank of England. It corresponds to the item "reserve funds" in the Balance Sheets of other banks, with this difference, that the profits are added to the rest from time to time, and the dividends of the Bank proprietors are paid out of this account. It is the practice of the Bank of England to take care that the rest does not fall below £3,000,000. The term "rest" is applied in another sense to the break which a banker makes in the accounts of his customers, at the end of June and December respectively for the purpose of entering the amount of the interest and the charges which are due to date. The account is balanced and ruled off as soon as this is done, and the balance is carried forward to the account of the next half-year.

RESTRAINT OF TRADE.

Contracts are said to be in restraint of trade when any restriction is imposed of any character whatsoever. By the common law, if the restraint was general, the contract was null and void. But in recent times, although possibly a total restraint of trade would still be held to be a contract which the law would not enforce, it has come to be recognised that a partial restraint is permissible, provided that the restraint is not contrary to the public interest, and that under the circumstances it is just and equitable. Again, no contract in restraint of trade, even though made under seal, is valid unless it is supported by some valuable consideration. It is in respect of the necessity for a consideration that a deed which refers to a contract of this kind differs from every other kind of deed.

The reasons for holding contracts in general restraint of trade void may be concisely stated in the words of an old case which dealt exhaustively with the matter—

"(1) Such contracts injure the parties making them, because they diminish their means of

procuring livelihoods and a competency for their families. They tempt improvident persons, for the sake of gain, to deprive themselves of the power to make future acquisitions. And they expose such persons to imposition and oppression.

"(2) They tend to deprive the public of the services of men in the employments and capacities in which they may be most useful to the community as well as to themselves.

"(3) They discourage industry and enterprise, and diminish the products of ingenuity and skill.

"(4) They prevent competition and enhance prices.

"(5) They expose the public to all the evils of monopoly."

It must be obvious that it would be absolutely impossible to lay down any rules which would exactly meet the circumstances of every case. The first great factor is the nature of the business. Some businesses are merely local, others are world-wide. Clearly the limitations of space and time in the case of the former must be greater than in the case of the latter. And the second great factor is the number of likely customers. This was one of the points which had so much weight in the leading modern case upon the subject, namely, *Nordenfjell v. Maxim Nordenfjell Guns and Ammunition Co.* (1894, A.C. 535). There, a patentee and manufacturer of guns and ammunition for purposes of war covenanted with a company, to which his patents and business had been transferred, that he would not for 25 years engage, except on behalf of the company, either directly or indirectly, in the business of a manufacturer of guns or ammunition. It was held that, although the covenant was unrestricted as to space, yet, having regard to the nature of the business and the limited number of customers, namely, the Governments of this and other countries, it was not wider than was necessary for the protection of the company, nor injurious to the public interests of this country, and that it was, therefore, valid.

Old cases are really of little use in considering this question, for the rapid advances made in communication by the railway, the telegraph, and the telephone, have made it possible for business to be carried on at considerable distances where formerly the limitations were exceedingly great. If there is a restraint imposed, it must be definite in its terms. Uncertainty will defeat it. And then it must be considered whether it is a restraint which can be reasonably held to be fair towards all the parties concerned.

In modern time it has become a common practice, upon engaging an employee, for the employer to make it one of the terms of employment that the employee shall not, after leaving his service, enter into a similar kind of employment within a limited area for a certain period of

time. If the limitations are reasonable under all the circumstances, the restraint is quite good, and the employee will be bound by it. Of course, the consideration in a case of this kind is the salary paid to the employee. Recently, there has been a tendency to consider the position of the employee in a more favourable light than formerly, and the case of *Eastes v. Russ*, 1914, 1 Ch. 468, should be referred to.

Lastly, when a business is sold, the purchaser of the same, if he desires to guard his own interests, will take care to impose a restraint upon the vendor's trading in the same kind of business in such a manner as to be likely to be detrimental to the purchaser's interests. Without some such restraint, the purchase of the goodwill of a business might be an utterly worthless speculation. What has just been stated as to an individual vendor and purchaser is equally true in the case of a partnership or a joint stock company

RESTRAINT ON ANTICIPATION.

In almost every marriage settlement that has been made during the last century and a half, where any interest in the settled funds has been given to the wife, it has been the custom to insert a clause by means of which her right is exclusively confined to the income which is to be paid to her as and when it becomes due. The great object of a clause of this kind is to prevent a woman bargaining away her future accruing property in such a manner that she might reduce herself to a state of destitution. A clause of this kind is known as a "restraint on anticipation." There is no limitation as to the inclusion of a restraint of this character when the trust funds are provided from some other source than the married woman herself, but if it is she who provides a portion of the trust funds, the restraint, which binds her property so long as she is a married woman most effectively, will not be allowed to operate as against those persons who were her creditors prior to the date of the marriage.

By the Married Women's Property Acts, 1882 and 1893, a married woman can contract in respect of her separate property as though she were a *feme sole*, whether that property is actually in possession or is to fall due to her at some future date. If, on the other hand, being a married woman and being entitled to an income out of certain settled funds, there should be a restraint on anticipation contained in the settlement, she can never contract except in respect of money which she has actually in possession. Let us take the following illustration. A married woman has property or earns an income amounting to £200 a year. She can enter into any contract she likes, and since the Act of 1893, either the money that she has in hand or any future income becomes liable for the liquidation of the debt incurred. If, on the other

hand, an income of a similar amount is paid under a marriage settlement containing a clause of restraint, and the income is paid in quarterly sums of £50, any contract entered into by her with respect to any payment to be made out of these is void, and she is not liable for anything beyond the money that is absolutely her own separate property at the time when she enters into the contract. Of course, the quarterly sums become her separate property directly she receives the same. It must be most carefully borne in mind that the "restraint on anticipation" only occurs in the case of a married woman. Directly she becomes a widow it ceases to have effect, although the clause is revived if she re-marries, unless it is restricted to a particular marriage.

As the restraint was found to work disadvantageously in certain cases, it was provided by Section 39 of the Conveyancing Act, 1881, that the fetter could be removed on application to the High Court, if a sufficiently strong case could be made out.

Lastly, an alteration has been made in the law with regard to bankruptcy, and it is provided by Section 52 of the Bankruptcy Act, 1914, that "Where a married woman who has been adjudged bankrupt has separate property the income of which is subject to a restraint on anticipation the Court shall have power on the application of the trustee to order that during such time as the Court may order, the whole or some part of such income be paid to the trustee for distribution among the creditors, and in the exercise of such power the Court shall have regard to the means of subsistence available for the woman and her children."

RETAINER.

This word is used in several senses. In the first place it is the written authority given by a client to his solicitor under which the solicitor acts in any particular litigation which is on hand. There are cases in which a solicitor may be retained verbally, but it is very unwise to dispense with a written document in case difficulties arise. So long as the retainer lasts—and it need not apply to more than one transaction—the solicitor is bound to give his best care and skill to the client's particular business, and to enter into no bargain with the opposing client without authority. In return, he has a lien on the papers of the lay client, and he cannot be compelled to deliver up the same until his costs have been paid.

In the next place, the term retainer is given to the act by which a solicitor engages a barrister at the earliest possible opportunity to appear for a particular client in a particular case. When this retainer has been given the barrister cannot appear for any other party to the case, and in return he is entitled to a brief in every step in

the proceedings in Court whenever counsel is required. If a general retainer is given, the barrister is entitled to be employed in every case in which the client is engaged.

Lastly, the term retainer is applied to the right which an executor possesses of paying himself, in the administration of a deceased person's estate, any debt which was owing to him by the testator in priority to any other debts owed by the testator to creditors in an equal degree. It is immaterial that by so doing he swallows up the whole or a greater portion of the remaining assets and leaves only a small sum or nothing at all for the other creditors. And this right of retainer is exercisable even though the debt is statute barred owing to the Statute of Limitations. It cannot, however, be exercised if the debt is unenforceable by some statutory provision such as the Statute of Frauds.

RETIRED BILL OF EXCHANGE.

(See BILL OF EXCHANGE, RETIRED.)

RETURN OF ALLOTMENTS.

In order that full disclosures as to the financing of a company may be afforded to shareholders and to the public, the Companies Acts require that returns of allotment of shares shall be made from time to time to the registrar of joint stock companies. The requirements of the Acts in this direction are now fixed by Section 88 of the Companies (Consolidation) Act, 1908. The effect of this section is that where shares are issued in consideration of a cash payment a return must be made within one month from the allotment, the return showing the number and nominal amount of the shares allotted, the names, addresses and description of the allottees, and the amount paid or due and payable on each share. A similar return is required where shares are allotted in the whole or part for a consideration other than cash, and, in addition, a contract in writing duly stamped constituting the title of the allottee to the allotment, together with any contract of sale or for services or other consideration in respect of which the allotment is made, such contract being duly stamped. These returns are in addition to the list and summary required to be filed annually under Section 26, and default in complying with the provision is visited by a fine of not exceeding £50 for every day of default as against every officer knowingly party to it. Where, however, the default is an accidental omission the Court may in a proper case extend the time for making the necessary return. The form of the return is given on page 833.

RETURNED EMPTIES.

Where no charge is made for packages when goods are sent out, and empties are credited at

Number of
Certificate -----

"THE COMPANIES ACTS, 1908 to 1917."

RETURN OF ALLOTMENTS
OF

Limited,

from the $\frac{1}{2}$ ----- day of -----, 19 ,

to the ----- day of -----, 19 ,



A Companies' Fee Stamp of 6s. must be impressed here.

Made pursuant to Section 88, Subsection 1, of The Companies (Consolidation) Act, 1908.

(To be filed with the Registrar of Joint Stock Companies within one month after the Allotment is made.)

*Distinguish between Preference, Ordinary, or other descriptions of Shares.

*Number of the ----- Shares allotted payable in Cash -----

*Nominal Amount of the ----- "Shares so allotted" £ -----

*Amount paid or due and payable on each such "Share" £ -----

Number of "Shares allotted for a consideration other than Cash" } -----

Nominal Amount of the Shares so allotted : £ -----

Amount to be treated as paid on each such Share : £ -----

The Consideration for which such Shares have been allotted is as follows—

Presented for filing by -----

† NOTE.—In making a return of Allotments it is to be noted that—

1. When a return includes several Allotments made on different dates, the dates of only the first and last of such Allotments should be entered at the top of this page, and the registration of the return should be effected within one month of the first date.

2. When a return relates to one Allotment only, made on one particular date, that date only should be inserted and the spaces for the second date struck out and the word "made" substituted for the word "from" after the name of the Company.

(Reverse)

NAMES, ADDRESSES, and DESCRIPTION of the Allottees of Shares in ----- Limited.

SURNAME.	CHRISTIAN NAME.	ADDRESS.	DESCRIPTION.	Number of Preference Shares allotted.	Number of Ordinary Shares allotted.	Number of Deferred or Founders' Shares allotted.

Signature -----

Date ----- 19 . .

Officer -----

factory oncost, the whole making up the *total cost of production*. It is the usual practice to frame the Profit and Loss Account of a manufacturing business so as to show in Section I of the account the *prime cost of production*, the various items of *factory oncost* being shown in another section, along with standing, management, and general expenses.

In a merchanting concern—that is, a non-manufacturing concern—the prime cost shown in the Profit and Loss Account is the prime cost of the *sales* and is made up of—

(a) the stock on hand at the commencement of the period; plus

(b) the purchase of goods during the period; less

(c) the stock on hand at the close of the period.

DISTRIBUTIVE EXPENDITURE.—All expenses incurred in placing the commodities on the market and in dispatching and delivering them to the purchasers, are distributive expenses. This would embrace travellers' salaries, commission, and expenses, agents' commission, carriage outwards, maintenance and upkeep of horses and carts, and motor vans; carters' and drivers' wages, etc.

FINANCIAL EXPENDITURE.—Bank charges, loan interest, bank interest, discounts on sales and on bills and all expenses incurred in financing the business come under the term Financial Expenditure.

ADMINISTRATIVE EXPENDITURE.—Under this head fall all management and office salaries, office rent, rates, and lighting, and all general, incidental, and petty expenses. If a limited company, the fees paid to directors and auditors would be included.

The books of account should be so designed that a statement grouping these different classes of revenue expenditure could be prepared with the minimum of labour and in a reasonable length of time. Generally this is done by the use of suitable analysis columns in the subsidiary books of account.

The term "expenditure" covers expenses actually paid, those incurred and not yet paid, and also those accruing. Further, the term embraces the provisions made to cover the depreciation of the various assets of the undertaking.

A clear understanding of what constitutes an expense must be aimed at, particularly in the accounts of a limited company. One difficulty is in grasping the distinction between debenture interest and a dividend upon preference shares.

Money received under debentures (sometimes called Debenture Capital) is a debt owing by the company, and upon this debt interest, at an agreed rate, has to be paid. This interest is a financial *expense* and is in nature the same as any other

interest payable upon money borrowed. The holders of the debentures are creditors (generally secured creditors) of the company.

Holders of preference shares are not, as such, creditors of the company, but are members, and any return paid to them is a dividend and must be paid only out of profits. The fact that the rate per cent. of the return is fixed at a certain amount has led to some confusion and looseness in expression and given rise to the use of the term "interest upon preference shares." The dividend paid to the holders of preference shares is an allocation of net profit and is not an expense. Debenture interest is payable whether there is a profit or not; preference dividend is payable only if there is a profit left after meeting all expenses, including debenture interest.

Expenditure upon fixed assets should be carefully considered so as to ensure its correct treatment in the books and accounts. If the expenditure is in the repair or upkeep of the asset it is clearly a charge against revenue. If it is in renewing a part or the whole, again it is a charge against revenue. As a rule, however, a depreciation fund is built up out of revenue, and in that case the cost of renewals would fall as a charge against the depreciation fund, and the annual allocation to depreciation fund, a charge against revenue. If the expenditure is in extending and adding to fixed assets, the cost must not be charged against revenue, but added to the capital value of the assets.

It may happen that the annual charge to revenue for depreciation is found to be insufficient, as where an asset, say a motor van or a horse, has been sold at a figure under that at which it has been written down to in the books. In such a case, the difference or loss must be charged to revenue. It is a loss of capital which must be made good out of revenue and thus becomes "Revenue Expenditure."

The careful allocation of expenditure between capital and income is necessary in the accounts of a trust, particularly where the persons entitled to the capital fund are other than those enjoying the income of the estate. Revenue or income would have to be charged with the following items of expenditure—unless contrary to the provisions of the settlement—

1. The rates and taxes on the property producing the revenue.

2. The cost of ordinary outgoing in the way of repairs to preserve intact the settled property.

3. The cost of insuring the property if the property be productive.

4. The costs of a succession duty account in respect of the life tenant's interest in the estate.

5. Costs and expenses incurred in getting in and distributing the income of the trust.

REVENUE RECEIPTS.

Revenue receipts are receipts on account of income ; or in other words, all receipts which are not capital receipts are revenue receipts.

Thus, in the case of a business man, all items that would legitimately go to the credit of his Profit and Loss Account may safely be classed as revenue receipts.

But the revenue derived from the exercise of a business is not the only class of revenue receipt. There are two outstanding classes, and they are—

- (a) earned revenue ; and
- (b) unearned revenue.

By the terms "earned" and "unearned" is indicated the distinction between income or revenue derived from the exercise of a trade, profession or occupation, and that derived by the landlord or capitalist as compensation from another for the use of his property or capital.

Earned income or revenue arises either from the manufacture or sale of tangible property, or from fees, wages, salaries, or honoraria received in exchange for manual or mental labour, while under the term "unearned revenue" falls the receipts of rent, interest, and dividends. These earnings should be periodically gathered together into a summarised statement, so as to show the *total* and the *net* revenue of the recipient for the period.

When the statement is with regard to a trader or business it is usual to term it a Trading or Profit and Loss Account ; when that of a professional man, it would be termed a Profit and Loss Account or Income and Expenditure Account. When showing the revenue derived from the *investment* of capital it is usual to term the statement a Revenue Account or Income Account, although the term "Revenue Account" is used also by statutory companies, such as railways, gas and electric lighting, and similar concerns, for the Profit and Loss Account.

REVENUE AND PROFITS OF A MANUFACTURING BUSINESS.—A manufacturer earns no revenue or profit upon the goods manufactured by him until these goods have been sold. He can then ascertain the *gross* profit upon these sales. The *net* profit earned upon the sales cannot be accurately ascertained until the proceeds have been collected. This is owing to the possibility of bad debts and the cost of getting in the outstanding debts. It is the exception for all sales made during a period to be converted into cash *during that period* and as a consequence the net profit brought out in a Profit and Loss Account represents the approximate *net* profit earned upon the sales and is subject to the Book Debts ultimately realising the amount at which they are valued at the close of the period. By making a provision

for bad debts and for discount it is possible to bring out a net profit very closely approximating to the actual net profit, and sufficiently near to meet all practical purposes.

The *gross* profit upon goods sold is the margin left between the prime cost of the goods sold and the price obtained from the purchaser. The *net* profit is the balance of profit left after providing for all fixed and standing charges, administrative and distributive expenses, depreciation of fixed and floating assets, and all expenses incurred during the period in earning the profit and conducting the business.

A manufacturer's business is one having two distinct departments. There is the manufacturing department in which the raw materials are worked up into the finished product ready for sale. Then there is the selling department in which these goods are placed upon the market and converted into money. As a general rule the manufacturing department transfers (or sells) the finished article to the selling department at *prime cost*, and the majority of manufacturing Profit and Loss Accounts are drawn up on this understanding. Some manufacturers, however, put a profit upon the finished goods before transferring them to the selling department, and when that is done, the Profit and Loss Account is so drawn up that the gross profit upon manufacture is shown separately from the gross profit upon the sale. To effect these results, it is necessary to draw up the Profit and Loss Account in sections, the separate sections showing the following particulars—

Section I. This would show upon the *debit* side—

- (1) the prime cost of the period's production and manufacture ; and
- (2) the gross profit upon the manufacture ; and upon the *credit* side the price at which the manufactured goods have been transferred to the selling department.

Section II. This would show on the *debit* side—

- (1) the prime cost of the goods sold (the prime cost being the price at which they had been taken over from the manufacturing department) ; and
- (2) the gross profit upon the sales ; and upon the *credit* side the sales.

Section III. This would show on the *debit* side—

- (1) all fixed and standing charges, administrative and distributive expenses, depreciation of fixed and floating assets, and all expenses incidental to carrying on the business ;
- (2) the net profit (if any) ; and on the *credit* side—
- (1) the manufacturing gross profit ;
- (2) the gross profit upon the sales ;
- (3) other items of income (if any) ;
- (4) the net loss (if any).

REVENUE RECEIPTS OF A MERCHANT'S BUSINESS.—A merchant's revenue or profit is derived from the resale of goods purchased by him for that purpose.

In the periodical Profit and Loss Account of a merchant's business the summary of his trading should be shown in sections similar in purpose to those of a manufacturer, with the exception that there would be no item for "prime cost of production" inasmuch as the merchant purchases but does not produce or manufacture the goods he sells. Consequently, Section I would show at the *debit*, (a) the prime cost of the sales; (b) the gross profit on the sales; and at the *credit*, the sales; and Section II would contain items corresponding to those in Section III of a manufacturer's Profit and Loss Account.

REVENUE RECEIPTS DERIVED FROM THE EXERCISE OF A PROFESSION.—These revenue receipts are mainly from fees charged to clients, although in some professions—doctors and dentists—revenue is obtained from the sale of commodities.

The Profit and Loss Account or Income and Expenditure Account in this case would show on the credit side, divided under suitable heads, all items of revenue for the period, and on the debit side all charges and expenses incurred in earning these items. The balance will represent net income or net loss. There would be included as part of the revenue for the period, an estimated sum for the fees earned but not yet rendered, such estimate being based upon a valuation of actual services rendered and not by guesswork or the inclusion of an arbitrary sum.

REVENUE RECEIPTS ARISING OUT OF THE INVESTMENT OF CAPITAL.—Under this head fall the rents received by a landowner for the use of his land, the rents received by a property owner for the occupation of his property, the interest received by a capitalist upon the investment of his capital in concerns conducted by others.

The revenue in these cases is acquired not by the personal exertions of the owners, but by the *lending* of their property or wealth to another. The periodical statement in this case is termed a Revenue or Income Account, and contains on the credit side the various rents or interests received and accrued, and on the debit side the expenses incurred in collecting and administering these sums. The balance is net revenue, or if the expenses exceed the gross revenue, a deficiency on Revenue Account for the period.

The Income Account of a deceased's estate held in trust is a good example of this form of Revenue Account, and a clear conception of what constitutes revenue receipts and of what constitutes capital receipts is of the first importance.

The rules laid down in the Apportionment Act,

1870, and settled cases (and referred to in the article on CAPITAL RECEIPTS) must be strictly adhered to.

REVENUE RECEIPTS OF A MUNICIPALITY OR PUBLIC BODY.—The revenue of a municipality is derived from numerous sources, such as property rents, fees or fines, licences, government grants towards education and police administration, sales of materials; and, as these are insufficient to meet the necessary municipal expenditure, the balance is obtained—

(1) From allocations of profits earned by the trading departments (tramways, electricity and gas supply, water, etc.); and

(2) the rates levied upon the community.

REVENUE RECEIPTS OF THE GOVERNMENT are obtained from taxes, customs and excise duties, estate and legacy duties, and the profits of the various Government departments.

The Allocation of Revenue Receipts is guided (except in the case of an individual) either by Agreement or by Statute or Case Law. In a partnership the Articles or Agreement of Partnership would define the respective partners' rights; if there is no agreement, the revenue receipts belong to the partners in equal shares. The revenue receipts of a limited company are subject to the regulations contained in its Articles of Association.

An important and interesting decision of the Court of Appeal is that in *Lee v. Neuchatel Asphalte Co., Ltd.* By the Articles of Association of this company, the net profits were to be applied first in paying a dividend at the rate of 7 per cent. per annum on the preferred shares, thereafter a dividend at the rate of 7 per cent. per annum on the ordinary shares, and if any surplus net profits remained they should be divided rateably amongst the shareholders without discrimination between classes of shares. There was further a provision to the effect that the directors were not bound to form a fund or otherwise reserve moneys for the renewal or replacement of any lease, or the company's interest in any property or concession. It was held that the total revenue receipts after meeting the current expenditure were, so long as the capital of the company remained intact, available for distribution among the shareholders and that it was not necessary to set any portion apart as a reserve or depreciation fund for replacing the wasting assets. The asset in which the capital was originally invested would naturally become exhausted and the fixed capital would therefore appear to be lost. But if the excess receipts have been periodically distributed amongst the members (and no provision made for replacement of the wasting asset) each distribution will, in effect, contain a repayment of capital, and will not really be, although nominally it is stated to be, net revenue.

REVERSION.

When a grant of an estate has been made to a person for a limited period, or when the holding of an estate is made terminable upon the happening of some specified event, the estate which remains and falls again into the possession of the grantor is called the reversion. Thus, if the tenant in fee simple makes any grant in favour of another, either for life or for years, or even in fee tail, the residue of the estate, that is, the portion not dealt with after the time for which the grant was made, reverts to the grantor, and so long as the grantee is not actually in possession he has what is known as an estate in reversion. If, at the time when the estate is thus carved out, this reversion is granted to some third person so as to make him entitled when the estate carved out comes to an end, it is called a "remainder." (See also EXECUTORSHIP ACCOUNTS, p. 453; REMAINDER.)

REVERSIONARY INTEREST.

The interest in an estate which is taken by a person who is entitled to the reversion (*q.v.*).

REVOCATION.

(See WILLS.)

ROLLING STOCK.

A Rolling Stock Account should be opened for the purpose of charging the initial cost of rolling stock, which then appears in the balance sheet as an asset. This class of asset is subject to constant repair, and provided the cost of such repair is properly charged against revenue, it is only necessary to write off from $7\frac{1}{2}$ per cent. to 10 per cent. on the diminishing value for depreciation, the rate varying according to the nature of the rolling stock.

In this connection the auditor should carefully examine the invoices to see that only actual additions or replacements of stock which has been completely written off by depreciation charges, are capitalised. He should also require the production of a schedule of the rolling stock, duly certified by the manager or other responsible party to be in an efficient condition. By comparing this schedule with similar schedules for previous periods, he will be able to verify the maintenance of the quantity of stock and to check any additions to capital by increases revealed in the schedules.

ROOT OF TITLE.

(See ABSTRACT OF TITLE.)

ROYALTIES.

Royalties are the agreed amounts payable to owners of certain rights or commodities for a

right of user, or in consideration of other privileges granted by such owners. The more common instances of royalties are as follows—

1. By the publisher of a book to the author at an agreed rate on every copy of such book published or sold.

2. By a manufacturer or retailer to a patentee, either at an agreed rate on every article made or sold under the patent (the rate being fixed or varying with the price obtained for the article) or by a percentage on the actual profits earned by the manufacturer or retailer.

3. By the lessee of a colliery, mine, or quarry to the lessor (also known as the surface owner) for the privilege of "getting" minerals from the property. The royalty in such cases is either calculated on a fixed sum per ton of minerals obtained or per cubic yard or acre worked, arrived at by a periodical measurement by a Surveyor agreed upon by both lessor and lessee, or upon a sliding scale based upon the prices obtained for the mineral. The agreement between the lessor and lessee usually stipulates for a certain fixed minimum amount per annum payable irrespective of the quantity of mineral raised. This fixed amount is called the minimum or dead rent.

The excesses of the minimum or dead rent over the royalties computed in any one year on the basis of the mineral raised or acreage worked are termed "short workings," or "shorts." In the case of mines in course of development, the minimum rent may for some time exceed the actual royalties based on quantities. Most leases grant the lessee the right to recoup himself for such "shorts" out of the excess of actual royalties, if any, in any one year, within a certain stipulated time. In such cases the short workings may be temporarily capitalised and treated as a nominal asset. The asset is reduced by the amount of excess royalties until the short workings are completely recouped, after which the whole of the excess royalties are payable to the lessor. At the expiration of the stipulated time the balance, if any, of the "short workings" nominal asset should be written off as an ascertained loss. Short workings should only be capitalised, even temporarily, where the lessee is satisfied that he will be able to recoup himself within the period, either by reason of the quantity of mineral to be raised or by the length of the lease.

As regards ordinary royalties, the book-keeping is simple, consisting of entries in the Journal in respect of royalties due and entries in the Cash Book in respect of cash received, and the usual Ledger accounts.

In the case of short workings, the accounts should be kept as shown by the following illustration—

A colliery is leased by the "G. Co., Ltd.," from "Lord Z.," subject to a royalty of 1s. per ton of

coal raised, with a minimum rent of £1,500 per annum, and power to recoup short workings out of subsequent surplus royalties within a period of five years from 1st January, 1915. In the first four years the amount of coal raised was respectively—

1915	.	.	18,000	tons
1916	.	.	26,000	"
1917	.	.	38,000	"
1918	.	.	50,000	"

The Journal entries to be made in the books are as follows—

Debit Minimum Rent Account and credit Lord Z. with the amount of the minimum rent or the instalment due in accordance with the lease.

Debit Royalty Account and credit Minimum Rent Account with the royalties, as ascertained periodically. It is convenient to make up the royalty returns to the date at which the instalments of minimum rent become due.

Debit Short Workings Account and credit Minimum Rent Account with the shortage on Minimum Rent Account.

Debit Coal Mining Account and credit Royalty Account with the actual royalties.

The following *pro forma* Royalty Accounts show the working out of the results in the books of the

G. Co., Ltd., for four years. For the sake of simplicity, it is assumed that the minimum rent is due and payable once a year, viz., on 31st December. It will be observed that by 31st December, 1918, the short workings in previous years had been recouped, and that there was a surplus of royalties over Minimum Account amounting to £600 payable to Lord Z. (See forms of account below.)

INCOME TAX ON ROYALTIES.—Income Tax must be deducted from the minimum rent or the royalties when paid, pursuant to the rules of the Inland Revenue to collect tax from income at the source whenever possible.

It was decided in *re Broughton Co.*, 1884 (*Q.B.D.*), that although tax had been deducted by the lessee before payment of the minimum rent, the lessee must also pay tax upon such of the short workings as were subsequently recouped out of royalties in excess of the minimum rent. The Inland Revenue clearly receives tax twice over in respect of such short workings.

In many cases leases and royalty agreements provide that in the event of the bankruptcy of an individual or the liquidation of a company, as the case may be, the rights of the lessee under the leases or agreements automatically cease. (See also AUDITING, p. 80 ; TRADING ACCOUNT, p. 918.)

Dr.		THE RIGHT HONOURABLE LORD " Z "						Cr.		
		£	s.	d.			£	s.	d.	
1915.					1915.					
Dec. 31	To Cash	1,500	0	0	Dec. 31	By Minimum Rent A/c .	1,500	0	0	
1916.					1916.					
Dec. 31	To Cash	1,500	0	0	Dec. 31	By Minimum Rent A/c .	1,500	0	0	
1917.					1917.					
Dec. 31	To Cash	1,500	0	0	Dec. 31	By Minimum Rent A/c .	1,500	0	0	
1918.					1918.					
Dec. 31	To Cash	2,100	0	0	Dec. 31	By Minimum Rent A/c .	1,500	0	0	
					Dec. 31	By Balance transferred from Minimum Rent A/c	600	0	0	

MINIMUM RENT ACCOUNT

		£	s.	d.			£	s.	d.
1915.					1915.				
Dec. 31	To Lord "Z"	1,500	0	0	Dec. 31	By Royalty A/c	900	0	0
1916.					" 1916."	" Short Workings A/c .	600	0	0
Dec. 31	To Lord "Z"	1,500	0	0	Dec. 31	By Royalty A/c	1,300	0	0
1917.					" 1917."	" Short Workings A/c .	200	0	0
Dec. 31	To Lord "Z"	1,500	0	0	Dec. 31	By Royalty A/c	1,900	0	0
" "	" Short Workings A/c .	400	0	0					
1918.					1918.				
Dec. 31	To Lord "Z"	1,500	0	0	Dec. 31	By Royalty A/c	2,500	0	0
" "	" Short Workings A/c .	400	0	0					
" "	" Lord "Z" Balance .	600	0	0					

Dr.		ROYALTY ACCOUNT						Cr.		
1915. Dec. 31	To Minimum Rent A/c— 18,000 Tons @ 1/- .	£ 900	s. 0	d. 0	1915. Dec. 31	By Coal Mining A/c .	£ 900	s. 0	d. 0	
1916. Dec. 31	To Minimum Rent A/c— 26,000 Tons @ 1/- .	1,300	0	0	1916. Dec. 31	By Coal Mining A/c .	1,300	0	0	
1917. Dec. 31	To Minimum Rent A/c— 38,000 Tons @ 1/- .	1,900	0	0	1917. Dec. 31	By Coal Mining A/c .	1,900	0	0	
1918. Dec. 31	To Minimum Rent A/c— 50,000 Tons @ 1/- .	2,500	0	0	1918. Dec. 31	By Coal Mining A/c .	2,500	0	0	

SHORT WORKINGS ACCOUNT

1915. Dec. 31	To Minimum Rent A/c .	£ 600	s. 0	d. 0	1915. Dec. 31	By Balance . . .	£ 600	s. 0	d. 0
1916. Jan. 1	To Balance . . .	600	0	0	1916. Dec. 31	By Balance . . .	800	0	0
Dec. 31	To Minimum Rent A/c .	200	0	0	1917. Dec. 31	By Minimum Rent A/c .	400	0	0
1917. Jan. 1	To Balance . . .	800	0	0	1917. Dec. 31	By Balance . . .	400	0	0
1918. Jan. 1	To Balance . . .	400	0	0	1918. Dec. 31	By Minimum Rent A/c .	400	0	0

SALARIES AND WAGES.

THE treatment of salaries and wages in the books of account depends largely upon the nature of the work for which the salaries and wages are paid. In the case of manufacturing concerns, the wages paid to workmen and the salaries paid to officials, who are directly engaged in the productive departments may, with advantage, be kept distinct, by the use of a separate wages book, or by an analysis of wages, from those paid to persons engaged upon the distributive side of the business. By this means the manufacturing wages and salaries may be ascertained and charged to the Manufacturing Account, whilst the remainder can be charged to the Profit and Loss Account.

In verifying the payment of wages, the auditor has to rely largely upon the system of internal check in force in the preparation of the pay-roll and the subsequent disbursement of the wages to the workpeople. The pay-roll should pass through as many hands as can conveniently be arranged. The time and rates of payment should be written up by one clerk, and the calculations and additions made by another. A third clerk should check them, and the actual payment should be made by some responsible person who has had no hand in the preparation of the Wages Book. The time sheets should be certified by the foreman. The rates of pay should be examined and certified by the manager, whilst each clerk should sign the Wages Book for the actual work he has done upon it, and for which he is responsible. The duties of the clerks may, with advantage, be changed from time to time. The auditor should test the extensions and castings and verify the totals with the cash paid out. He should see that all certificates are properly signed, and should assure himself from time to time that the system of internal check is properly carried out. He may, on occasion, attend at the time of paying the wages, and require an explanation of any apparently unclaimed wages. He should test the individual rates of pay by comparison and carefully watch the total amounts paid week by week, requiring a satisfactory reason for any undue increase. (See also AUDITING, p. 80, PROFIT AND LOSS ACCOUNT, p. 791.)

SALE NOTE.

(See CONSIGNMENT ACCOUNTS, p. 310.)

SALE OF ASSETS.

(See ASSETS, SALE OF.)

SALE OF GOODS ACT, 1893.

This is one of the codifying Acts dealing with the law relating to commercial matters, other important ones being the Bills of Exchange Act, 1882, the Factors Act, 1889, the Companies (Consolidation) Act, 1908, the Bankruptcy Act, 1914, and the Deeds of Arrangement Act, 1914. The present article will deal only with the more important provisions of the Statute. All the ordinary rules of contract, such as offer and acceptance, the capacity of the parties, consideration, good faith, etc., apply to sale as to other contracts.

A sale of goods is defined as a contract whereby the seller transfers or agrees to transfer the property in the goods, the subject matter of the contract, to the buyer for a money consideration called the price. By "property" is meant the complete ownership in the goods, and "goods" include all chattels personal other than *choses in action*. In order that a contract of sale may fall within the Statute, it is essential that the whole of the rights of the seller should be intended to be passed on to the buyer, and some part of the consideration must be money. If the consideration consists of some other goods, the contract is one of barter, and the Act does not apply. If the goods are transferred without a consideration, the transaction between the parties is a gift.

When the sale is carried out at once, that is, when the seller hands over the goods and the purchaser pays the price, no formalities are required. But when the contract is executory, that is, when the transaction is to be carried out at some future time, the sale is not enforceable by action, if the value of the goods is £10 or upwards, unless (a) something is given in earnest to bind the contract, or (b) part payment is made, or (c) a note or memorandum in writing is made and signed by the party to be charged. This note or memorandum must contain the names of the parties to the contract, that is, the seller and the buyer, and the terms of the contract in full, and it must be signed. No stamp duty is required in the case of an ordinary memorandum. If, however, a deed is utilised—for which there is really no necessity—a 10s. duty is payable.

When the purchaser of goods has a full opportunity of examining the same, there is no implied warranty or condition as to the quality or fitness of the goods for any particular purpose in the absence of any statutory provision as to the same. The maxim "*caveat emptor*" (*q.v.*) applies,

Conditions and Warranties. The Act defines a warranty as "an agreement with reference to goods which are the subject of a contract of sale, but collateral to the main purpose of such contract, the breach of which gives rise to a claim for damages, but not the right to reject the goods and treat the contract as repudiated." Condition is not defined in the Act, but it is of the essence of the contract. The terms "warranty" and "condition" are often confused. Any express statement as to the nature and quality of the goods may be made by the seller, and, if made, the seller is bound by his warranty, but in the absence of any express stipulation, the law implies certain warranties, not only as to quality and fitness, but also as to title, unless the same are particularly excluded by the terms of the contract. As far as title is concerned, there is an implied condition that the seller has a right to sell the goods, and a warranty that the same are freed from all incumbrances. This implies that the buyer, when he obtains possession of the goods, shall not be subjected to any claim by a third party. But if the sale is made by a sheriff or by a pawnbroker, the warranty only extends to this, that the seller was not aware of anything which affected the title to the goods in a prejudicial manner and then the buyer takes the same rights as were enjoyed by the seller at the time of the contract.

As regards quality or fitness, a condition is implied, unless expressly excluded, in the following cases—

(a) When goods are sold by a trader for a particular purpose, of which he is well aware, and it is shown that the buyer relies upon the skill or judgment of the seller, the goods must be reasonably fit for the purpose for which they are intended. This is so whether the seller is the manufacturer or not, but there is no implied warranty of quality or fitness if a specific article is sold under its patent or trade name.

(b) When the contract is for the supply of manufactured goods they must be of merchantable quality. And this condition is not excluded by the fact that the goods are sold by sample.

(c) When the sale is by sample, in addition to the above-mentioned implied condition that the goods are merchantable, there are added the two following—

1. The bulk shall correspond with the sample in quality.

2. The buyer shall have reasonable opportunities for comparing the bulk with the sample.

(d) By the custom of a particular trade it may be shown that there is an implied warranty upon the sale of goods connected with that trade. This is entirely a question of evidence.

(e) By the Merchandise Marks Act, 1887, a

warranty of genuineness is implied from a trade mark or description.

(f) By the Fertilisers and Feeding Stuffs Act, 1893, the seller of manufactured or artificially prepared fertilisers or feeding stuffs is bound to give a particular invoice to the buyer, and this invoice has the effect of a warranty of the statements contained in it. Also on the sale of an article for use as cattle food, there is an implied warranty by the seller that the article is fit for feeding purposes.

(g) By the Chain Cables and Anchors Act, 1894, on a contract for the sale of a chain cable there is an implied warranty that it has been properly tested and stamped.

Very frequently a contract of sale is entered into subject to certain special conditions. If the conditions are not fulfilled, the buyer has the right to repudiate the contract altogether, and not merely to claim damages, which is his usual remedy when there is a breach of a warranty. It is not always easy to distinguish a condition from a warranty. This is, however, a matter of evidence.

Transfer of Property. As the owner of property is always the person upon whom the loss must fall if the goods which have been sold are destroyed, it is of the utmost importance to fix the rules as to the time when the property passes from the seller to the buyer. In the absence of any special stipulation in the contract as to when this takes place the Act supplies the following rules—

(a) Where there is an unconditional contract for the sale of specific goods which are ready for delivery, the property passes to the buyer when the contract is made. The fact that the time of payment or delivery is postponed is immaterial.

(b) Where there remains something to be done by the seller in order to put the goods into a deliverable state, or where the goods have to be measured, weighed, or tested, the property does not pass until the act required is done and notice of it has been given to the buyer.

(c) Where goods are delivered to the buyer on approval, or "on sale or return," or on other similar terms, the property passes to the buyer as soon as he approves of them, or does some act showing his adoption of the transaction; and he will be presumed to have approved of the goods if he retains them, and gives no notice of rejection within a reasonable time.

(d) Where there is a contract for the sale of unascertained or future goods by description, and goods of that description in a state ready for delivery are unconditionally appropriated to the contract by either party with the express or implied assent of the other, the property in these goods passes at once to the buyer. Such an

appropriation is made when the goods are delivered to a carrier for transmission to the buyer.

(e) Where there is a reservation by the seller of the right of disposal of the goods until certain conditions are fulfilled, the property in the goods will not pass until the conditions have been fulfilled, notwithstanding the delivery of them to the buyer, or to some other person on his behalf.

Transfer of Title. If the goods are transferred by any person other than the owner or his agent, the buyer cannot acquire any better title than that which the transferor had, unless there is some statutory enactment to the contrary, as, for example, the Factors Act, or unless the goods transferred are negotiable instruments. In the former case the transferee may become the absolute owner if the transfer is made in the ordinary course of business, whilst if the transaction is *bonâ fide* the transferee is always the rightful owner of a negotiable instrument. The chief exception to the rule that a transferee obtains no better title than that which the transferor possessed is the case of the sale of goods in "market overt" (*q.v.*). It is always advisable for the purchaser of goods to obtain possession of the same or the documents of title referring to them at the earliest possible moment. Otherwise, if either the goods or the documents of title to them are outstanding, there may arise difficulties through another transfer and the purchaser may be left without any effective remedy.

Performance of the Contract. The chief duty of the seller is to deliver the goods, and that of the buyer is to accept the same in accordance with the terms of the contract. Unless there is some stipulation to the contrary, the buyer is bound to pay for the goods at the time of delivery. Again, the seller is under no obligation to convey the goods to the buyer, unless he has undertaken to do so. It is quite sufficient if he gives notice to the buyer that the goods are at his disposal and provides reasonable facilities for his taking possession of them. When, however, the seller undertakes to deliver, it is sufficient if he makes delivery to a carrier to convey them to the buyer; but notice of the fact of delivery to a carrier must be given to the buyer so that the latter may insure them. In making delivery, the seller must send the exact quantity of goods ordered. If he delivers either more or less, the buyer has the option of refusing or of accepting them; but if he accepts them, he must pay for the quantity accepted, whether more or less than the quantity ordered, at the contract rate. In the absence of any agreement to this effect, the buyer is not bound to accept delivery by instalments.

Lien of the Seller. For any breach of the contract of sale, the buyer and the seller have a personal remedy, the one against the other. But in addition to the personal remedy a seller has

certain rights against the goods themselves, even though the property in them may have passed to the buyer, so long as the actual possession of them remains with the seller.

The first of these rights is "lien" (*q.v.*). The seller of goods, who has not been paid, is entitled to retain possession until the price has been paid or tendered, when—

(1) The goods have been sold without any stipulation as to credit; or

(2) The period of credit has expired; or

(3) The buyer has become insolvent.

But the lien will be lost—

(1) If the goods are delivered to a carrier to be sent to the buyer, and the seller does not reserve the right of disposal; or

(2) If the buyer or his agent obtains possession of the goods; or

(3) If the right is waived by the seller.

Another right of the seller* is that of re-taking possession of the goods under certain conditions whilst they are on their way to the buyer. (See **STOPPAGE IN TRANSITU.**)

Right of Re-Sale. An unpaid seller has the right of re-sale when the buyer, within a reasonable time, refuses to pay for the goods or to tender the price of them.

It arises in three cases—

(a) Where the goods are of a perishable nature;

(b) Where the seller has given express notice of his intention to re-sell, and the buyer does not tender the price;

(c) Where the seller has reserved to himself a right of re-sale in case of the default of the buyer.

Remedies of the Seller. If the property in the goods sold has passed to the buyer, in accordance with the rules already stated, and the buyer either refuses to accept the goods when tendered to him, or to pay for them when they have come into his possession, the seller has a right of action, in the first case for damages for non-acceptance, and in the second for the price of the goods. The measure of damages for non-acceptance is the estimated loss which directly and naturally results from the buyer's breach of contract. This is ascertained, when there is an available market for the goods in question, by the difference between the contract price and the market or current price at the time when the goods ought to have been accepted. When an action for the price is contemplated, no proceedings can be taken until the money is actually due. In certain special cases interest may be allowed in addition to the price of the goods.

A bill of exchange given in payment of goods operates generally as a conditional payment. If the bill is dishonoured at maturity the debt

revives, and the seller may sue either upon the bill or upon the consideration for the sale.

Remedies of the Buyer. When the seller wrongfully neglects or refuses to deliver the goods according to the terms of the contract, the buyer may maintain an action against him for damages for non-delivery. The measure of damages, as in non-acceptance, is the estimated loss which directly and naturally results from the seller's breach of contract. This is also ascertained in the same way as in the converse case of non-acceptance. But special circumstances may enhance the damages, especially if there is no available market in which the buyer can obtain similar goods, or if he has made known to the seller the fact that the goods are required for a

SALES ACCOUNT.

An account kept in the Nominal Ledger, which is credited with the periodical totals of goods sold, as per Day Books, and debited with the periodical total of goods returned, allowances, etc., as per Inwards Returns and Allowances Book. The balance gives the net sales, and is transferred on balancing from the Sales Account to the credit of the Trading Account.

The Sales Account may be kept in columnar form for the purpose of ascertaining departmental sales, separate Day Book and Returns Book being used for each department, or these books correspondingly departmentalised by means of analysis columns.

Dr.		SALES ACCOUNT												Cr.					
		Total.		Clothing Dept.		Boot Dept.		Out-fitting Dept.				Total.		Clothing Dept.		Boot Dept.		Out-fitting Dept.	
		£ s. d.		£ s. d.		£ s. d.		£ s. d.				£ s. d.		£ s. d.		£ s. d.		£ s. d.	
19..										19..									
Mar. 18	To Returns per Inwards Rets. Book	19	6 8			18	4 0	1	2 8	Jan. 31	By Sundries per Sales Day Book	102	17 4	29	17 11	54	3 11	18	15 6
Apr. 28	" " "	18	2 9	17	4 9			18	0	Feb. 28	" " " "	91	0 1	36	4 0	32	7 9	22	8 4
June 30	To Transfer to Trading A/c	552	0 10	174	9 2	247	9 3	130	2 5	Mar. 31	" " " "	101	4 4	24	1 6	47	2 1	30	0 9
										Apr. 30	" " " "	104	12 1	42	4 1	38	3 0	24	5 0
										May 31	" " " "	89	2 9	27	4 9	42	13 6	19	4 6
										June 30	" " " "	100	13 8	32	1 8	51	3 0	17	9 0
		£589	10 3	191	13 11	265	13 3	132	3 1			£589	10 3	191	13 11	265	13 3	132	3 1

particular purpose. Each case, however, will depend upon its own circumstances.

When the goods sold are of peculiar value, the Court may, if it thinks fit, order the seller to deliver the identical goods he has contracted to supply, that is, may decree what is called specific performance (*q.v.*) instead of condemning him in ordinary damages.

Where there is a breach of warranty by the seller, or where the buyer elects, or is compelled to treat a breach of a condition on the part of the seller as a breach of warranty, the buyer is not entitled, merely by reason of such breach, to reject the goods, but he can set up the breach in diminution or extinction of the price, or he can maintain an independent action against the seller for damages for breach of warranty. In the case of breach of warranty of quality, the damage sustained is the difference between the value of the goods at the time of delivery to the buyer and the value they would have had if they had answered to the warranty. (See also ACCEPTANCE AND RECEIPT.)

SALE OR RETURN.

(See GOODS ON APPROVAL.)

SALES.

(See AUDITING, p. 75; TRADING ACCOUNT, p. 914.)

SALES BOOK.

This is the book of original entry for all goods sold. It contains full detail respecting them, namely, order number, date, name of purchaser, goods mark, quantity, price and total; the total of each entry is posted to the debit of the respective Personal Accounts in the Debit Ledger. The book is totalled periodically, and this total is posted to the credit of Sales or Goods Account in the Nominal Ledger.

The invoice sent to the customer is a copy of the Sales Book entry; in fact, it is a common practice to use manifold books, the alternate pages being the printed invoices which may be torn out, and the manifold copies constituting the firm's Sales Book. This system may be still further extended to enable the order also being entered in duplicate, these being sent to the warehouse for execution. The warehouse retains one copy for the purpose of entering the Stock Books, sending the other, with all particulars noted thereon, back to the office. The two remaining copies (*i.e.* customer's invoice and Sales Book entry) are then completed from this information.

Where more than one department exists, the book may be detailed for the analysis of the sales

to the various departments, and in this case the totals of the analysis columns are posted to the credit of the Departmental Sales Accounts, which may be one account in columnar form, in the Nominal Ledger.

SCHEME OF ARRANGEMENT.

A proposal made by a debtor in the course of bankruptcy proceedings. (See DEED OF ARRANGEMENT.)

SALES BOOK

						Cotton Prints.			Velvet.			Silk.			Wool-lens.			Fancy.		
			£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.
19..	April	3	T. Gould—																	
			14 pieces Blue Prints @ 10/6			7	7	0												
			11 " Velvet @ 15/-			8	5	0												
			40 yds. Velvet to pattern @ 2/6			5	0	0												
	"	4	J. Jameson—						20	12	0	7	7	0	13	5	0			
			40 doz. Flowers @ 6d.						1	0	0							1	0	0
	"	5	W. Booth—																	
			20 yds. Silk @ 3/11			3	18	4												
			14 " " @ 5/6			3	17	0												
									7	15	4			7	15	4				
	"	5	W. Venables—																	
			2 pattern books not ret'd. @ 2/6						5	0						5	0			
	"	7	K. Moon—																	
			4 yds. Prints, Fancy @ 4½d.						1	6		1	6							
						£29	13	10	£7	8	6	£13	5	0	£7	15	4		5	0
																		£1	0	0

SALES DISSECTION BOOK.

(See OFFICE ORGANISATION and SCHEMES OF INTERNAL CHECK.)

SALES LEDGER.

The Ledger which contains the Personal Accounts of all parties to whom goods are supplied, and, therefore, to which all items of goods sold are posted. The postings are made from the Sales or Day Books to the debit of the accounts, and from the Returns Inwards Book, Cash Book and Journal (for Bills Receivable) to the credit. The accounts are sometimes opened in alphabetical order, and in large concerns the Sales Ledger may be subdivided into a series : as Town, Country, Foreign, or/and A—D, E—G, etc., the entry of the Ledgers being thus expedited by the work being allocated amongst the staff. Should it be necessary to sub-divide the Ledger, sectional balancing principles should be inaugurated. (See also SELF-BALANCING LEDGERS, p. 846.)

SALES, PURCHASES, AND WAGES.

(See ACCOUNTS, CRITICISM OF, p. 13.)

SALES RETURNS BOOK.

(See SELF-BALANCING LEDGERS, p. 847.)

SALES TO BRANCHES.

(See BRANCH ACCOUNTS, p. 266.)

SAVINGS BANKS, AUDIT OF.

(See AUDITING, p. 100.)

SCHOOLS AND COLLEGES, AUDIT OF.

(See AUDITING, p. 118.)

SCRIVENER.

A person to whom money or other property is entrusted for the purpose of lending it out to others at interest payable to his principal. The remuneration of a scrivener is a bonus or a commission payable for his work and labour in connection with the transaction. The commission so paid is frequently spoken of as a "procuration fee."

SECRET RESERVES.

Secret Reserves may be created in the books of account (1) by the omission or under-valuation of assets; (2) by writing off excessive depreciation; (3) by over-stating liabilities; and (4) by charging capital expenditure to revenue. The chief object of secret reserves is the maintenance of steady dividends, and, in the case of banks, for instance, the avoidance of the disclosure of heavy and exceptional losses which might seriously affect credit. Where secret reserves have been determined upon, it is preferable to create a distinct Reserve Account in the books rather than to adopt the methods of creation set out above. By this means the actual real values of the assets are maintained in the books, although they may appear in the Balance Sheet at lower values, and

the danger of losing sight of assets which have been written down to nil is avoided.

The auditor's duty in this connection is a delicate one. On the one hand, where secret reserves exist, the Balance Sheet is not a true and correct representation of the company's affairs. On the other hand, the maintenance of a secret reserve may be essential to the well-being of the company. The auditor must take each case on its merits. Where the company's Articles provide that such a reserve may be created, and the auditor is satisfied that the creation of a secret reserve is *bonâ fide*, and in the interests of the company, he will probably not incur any liability if he omits to mention its existence in his report to the shareholders. In case of doubt, however, he would appear to have no option but to disclose the facts in his report. (See AUDITING, p. 90; BALANCE SHEET, p. 143; RESERVES AND RESERVE FUNDS, p. 826.)

SECTIONAL LEDGERS.

These are Ledgers containing a certain section of the accounts; for example, the Debit Ledgers may be sectionalised into Town, Country, and Foreign, or/and for the debtors whose names commence with certain letters of the alphabet, as A and B, C-E, F-H, etc.

When this is done, sectional balancing principles are usually adopted, so that errors may be localised to the ledgers in which they occur, a good system of internal check afforded, the total amount of outstanding balances known at any time without the trouble of abstraction from individual accounts, and final accounts more speedily prepared. (See also SELF-BALANCING LEDGERS, p. 846.)

SECURED CREDITORS.

(See BALANCE SHEET, p. 137; BANKRUPTCY ACCOUNTS, p. 161; LIQUIDATORS, ACCOUNTS OF, pp. 653 and 680.)

SECURITIES, AUDITORS AND.

(See AUDITING, pp. 96 and 99.)

SELF-BALANCING LEDGERS.

In all businesses of any magnitude, it is necessary to include in the system of book-keeping a number of ledgers, more particularly for the purpose of keeping the accounts with the debtors or creditors of the concern for goods sold or purchased. In order to reap the full benefit of the system where many such ledgers exist, the books should be so arranged that each ledger is self contained and can consequently be balanced without reference to any other ledger.

Unquestionably such an arrangement involves more clerical work, but the extra work and time occupied in posting and other detail work is amply repaid by the closer supervision which can be exercised and the greater facility with which

errors can be traced and detected and the books as a whole balanced.

In the case of concerns where operations cover a large area, and in the case of concerns trading in an article or commodity universally used, the number of ledger accounts is consequently considerable, and it is convenient to subdivide the sales ledgers alphabetically or according to district. For the purpose of facilitating reference, or of rendering the posting as simple as possible, alphabetical subdivision is the better, but where the undertaking depends largely for its sales upon the energies of a large staff of travellers, each one of whom is allotted a particular district, the ledgers may be divided according to districts. In such case a close control can be kept upon each traveller, not only regarding the total sales to the customers in his particular district, but also for the purpose of ascertaining the bad debts incurred amongst customers introduced by him.

It is usually found convenient to allot to each ledger a certain number of districts, the ledger being subdivided into sections in order that each district may have a certain number of pages allotted to it, each section therefore recording the accounts of the customers for whom a particular traveller is responsible.

In a business of magnitude each ledger clerk is made responsible for one particular ledger, and it is his duty entirely to complete the postings to his own ledger. Quite apart from other advantages which this method possesses, an interest is added to the work of each ledger clerk which, in practice, cannot but assist and expedite the otherwise monotonous and wearisome work of ledger posting. It will be found that, given the sole charge of a particular ledger, a ledger clerk is encouraged to give to his own work a greater attention to accuracy, neatness and general thoroughness, knowing that a quick and satisfactory balance of the ledger entrusted to his care will reap its own reward from the reports of the auditors to the chief ledger clerk.

In comparing a system involving self-balancing ledgers with a system with no such arrangement, it is apparent that the only disadvantage possessed by the former is the fact that more clerical work is involved by reason of the additional posting required and by reason of the analysis of the subsidiary books (explained below). Against this disadvantage may be summarised the following advantages.

ADVANTAGES OF SELF-BALANCING LEDGERS.—(1) As each ledger is capable of being balanced separately, the preparation of a total trial balance can be proceeded with without waiting until the whole system has been completed and balanced.

(2) Errors can be localised and the postings re-checked into the ledger or ledgers concerned.

(3) The total amount of the balances on any ledger may be ascertained with a minimum of delay and without the work involved in extracting the balances of the accounts in detail.

(4) Office organisation may be greatly assisted by the subdivision of clerks' labour.

(5) Statements to customers may be prepared and despatched and statements from suppliers checked with a minimum of delay.

(6) The possibility of fraud is lessened, particularly as it is in the knowledge of each clerk that, on detection of an error in posting, addition or balancing, or the questioning of the authority for the making of an entry in a subsidiary book and its subsequent posting, the clerk or clerks involved can be immediately ascertained.

In order to minimise the danger of collusion between clerks it is the practice in some concerns at irregular intervals to give instructions for all ledgers to be balanced and, on completion, the clerks are made responsible for ledgers other than the ones they have formerly kept. This practice acts as an effective deterrent on any incipient tendency towards fraudulent manipulations of the books on the part of any clerk who may feel himself particularly gifted in that direction.

Although a system of self-balancing ledgers may be applied to any business whatsoever, it is seldom that such a system obtains except where the nature of the business is such that a number of ledgers is necessitated to record the various transactions, such as a concern for the purchase (or manufacture) and the sale of goods in every day use. The examples in this article are of a system in such a concern.

ADJUSTMENT ACCOUNT.—It is obvious that, to render a ledger capable of being balanced separately, it is necessary to have a record of all items posted from subsidiary books to that ledger distinct from items of a similar nature posted to other ledgers. This record is obtained by a complete analysis of the items contained in the subsidiary books, or books of first entry. The totals of these analyses having been obtained, they are posted to an account which forms a "Control (or Adjustment) Account" for the ledger to which the details in the first place have been posted in the ordinary way. In this way the Control Account will be a summary of the ledger which it represents.

The Control Account for each ledger should be kept in a separate "Control Ledger" which, although not in itself an essential part of the system of books taken as a whole, yet is a necessary adjunct to each ledger if it be desired to balance each ledger separately.

The title "Self-Balancing Ledger" is in itself a misleading one in so far as it is necessary to refer to the particular Control Account in the

Control Ledger to obtain the total figures relating to any one ledger.

The term "Sectional Balancing System," which is a term referring to the same system, is, for this reason, a more suitable descriptive title.

In some concerns adopting the system it is the custom to keep the Control Accounts in the Private or Impersonal Ledgers.

This method is convenient, as the ledger then containing the Control Accounts is in itself a complete summary of all the ledgers.

One other method obtains also, which is to post the analysed totals of the subsidiary books both to a Control Account contained at the end of the ledger to which it relates on the opposite side to that to which the details of the analysis have been posted and also to a Control Account in the Private or Impersonal Ledgers as in the alternative method mentioned above.

The advocates of this method maintain that, to make each ledger strictly self-balancing, such a course is necessary, but obviously an additional amount of posting is involved which serves no useful purpose.

The use of the Control Ledger, which may be regarded as a Memorandum Ledger only, and which is used solely for the purpose of the various Ledger Control Accounts, is the one least open to objection, and theoretically more correct when it is borne in mind that the Control Accounts are not an essential part of a system of book-keeping, but are necessary only where it is desired to "prove" each ledger separately.

APPLICATION OF THE SYSTEM.—The following is the explanation of a system enabling the ledgers to be balanced separately in a trading concern with the following books—

- (1) Day Book (Sales).
- (2) Sales Returns Book.
- (3) Invoice Book.
- (4) Bought Returns Book.
- (5) Sales Ledgers.
- (6) Bought Ledgers.
- (7) Cash Book.
- (8) Petty Cash Book.
- (9) Bill Book.
- (10) Transfer Journal.
- (11) Impersonal Ledger.
- (12) Private Ledger.
- (13) Control Ledger.

(1) **Day Book.** This book is ruled in the ordinary way with columns for date, name and address, folio number and amount, but in addition it is ruled with as many columns as there are Sales Ledgers.

Form No. 1 (p. 847) shows such a Day Book for use in a concern with five Sales Ledgers. The Day Book is entered up in the usual way from the "Invoice Outwards Counterfoil or Copy Book" by the clerk responsible for this work, complete with all details as regards date, name and address, and the

amount charged to the customer for the goods, which is entered in the first or "Total" column. The Day Book is then taken by each ledger clerk in turn who posts up the debits to those customers' accounts contained in his ledger, entering in the folio column the initial or number of his ledger, and the folio; at the same time he extends the amounts posted by him to the proper column referring to his particular ledger.

Each clerk is responsible for totalling the column in the Day Book referring to his ledger.

At the end of each month the head clerk, or the clerk responsible for the posting of totals to the Impersonal or Private Ledgers, checks the "cross-casts," seeing that the totals of the analysis columns agree with the total of the "Total" column. The "Total" column is posted in the ordinary way by him to the credit of the Sales Account in the Impersonal Ledger.

Up to this point the procedure of posting is the usual one but, in addition, in order to complete the material for self-balancing, the total of each analysis column (representing the total of the debits to each Sales Ledger) is posted to the Debit of the Control Account in the Control Ledger referring to the Sales Ledger to which the details have been posted.

For the same reason the total of the "Total" column is posted to the credit of the "Impersonal Ledger Control Account" in the Control Ledger.

An alternative method as regards Day Books is to have a separate Day Book for each ledger, the great advantage where such a method is adopted being the fact that all the clerks may be engaged on posting at the same time, each using the Day Book referring to his own ledger and consequently not being obliged to wait until the posting to some other ledger than the one under his charge is completed.

The objections to this alternative method are that instead of one posting to the Impersonal Ledger (and to its Control Account) representing the total sales for the month, a number of postings is necessary, according to the number of Day Books. A greater objection to such a method is

that the clerk entering up the Day Books from the "Invoices Outwards" Counterfoil Book has to enter into a number of Day Books, and has himself to analyse the items of sale. In practice it is found that the former method explained above is safer, quicker and tends more towards accuracy, since the entering clerk has only to enter into the Day Book the particulars of sales as set out in the "Invoices Outwards" Counterfoil Book without the complication of analysis at the same time.

In any case it is extremely unwise to adopt the alternative method in a system where the Sales Ledgers are divided otherwise than alphabetically, as the responsibility of entering up the items into the proper Day Book is more than should be given to the ordinary entering clerk, and there is a great risk of items of sales being missed. The work of checking the entering, as can be easily appreciated, is necessarily complicated and slower.

Another system of arriving at the same result may briefly be touched upon. Under this arrangement the ordinary single column Day Book is used, the clerks inserting in the folio column the initial letter or number of their ledgers and the folio. At the end of each month, or at the end of whatever period at which the Day Book is totalled, a clerk extracts on a rough sheet the analysis of the items posted to the various ledgers, and the analysis so arrived at is copied into the Day Book showing how the total is made up. This method has no additional advantage to recommend it, and unless the distinctive initial or number denoting the ledger to which the item is posted is carefully written in, mistakes in the analysis frequently arise.

The only case in which this method should be brought into use is where no system exists for the separate balancing of ledgers, and where for some reason (for instance, where an error exists but cannot be located) it is required to prove the ledgers separately. In such a case there is no alternative but to proceed on the lines indicated. This question is discussed later.

(2) **Sales Returns Book.** This book is ruled in

Form No. 1.

DAY BOOK

Date.	Name and Address of Customer.	Ledger Folio.	Total.	Ledger 1.	Ledger 2.	Ledger 3.	Ledger 4.	Ledger 5.

an exactly similar manner to the Day Book, in fact the end of the Day Book may be utilised for recording the returns from customers, the procedure as regards posting being similar but converse. Details are posted to the credit of Customers' Accounts in the Sales Ledgers, the total of the "Total" column being posted to the debit of the Impersonal Ledger. To complete the self-balancing system the totals of the analysis columns are posted to the credit of the Sales Ledger Control Account in the Control Ledger, the total being posted to the debit of the Impersonal Ledger Control Account.

(3) **Invoice Book.** In the case of the majority of concerns the detail connected with the purchases is far less than that involved in the proper recording of the sales, and consequently one Bought Ledger is usually sufficient. In such cases, from a self-balancing point of view, the extra clerical work is very little and the necessary procedure is simple, following the converse lines of the system connected with the Sales Ledgers. The details of the Invoice Book are posted to the credit of the Bought Ledger Accounts, the total purchases going to the debit of the Purchases Account in the Impersonal Ledger. To complete the system the total is posted to the debit of the Impersonal Ledger Control Account, and to the credit of the Bought Ledger Control Account in the Control Ledger. Where more than one Bought Ledger is necessary the procedure is exactly similar to that obtaining in the case of Sales Ledgers. The Invoice Book is ruled, not only with a "Total" column but also with the necessary number of columns into which are extended the items according to the ledgers to which such items are posted, the totals of the analysis columns being posted to the credit of the Bought Ledger Control Accounts applicable.

In some concerns it is the custom not to enter the total of invoices into an Invoice Book, in which case it may be necessary to copy into the Invoice Book the complete detail of each invoice, or to file away the invoices for reference, but to gum the invoices into a guard book provided with a posting and folio column. The great advantage

of such a system is that the actual invoices are available for ready reference, and a very considerable amount of clerical work is avoided in copying out the details of each invoice. This method is, of course, equally applicable to a self-balancing system.

(4) **Bought Returns Book.** This book is dealt with obviously in a converse manner to the Bought Day Book. Details are posted to the debit of the Suppliers' Accounts in the Bought Ledger, the total being posted to the credit of the Purchases Account in the Impersonal Ledger. The total is again posted to the debit of the Bought Ledger Control Account in the Control Ledger, and to the credit of the Impersonal Ledger Control Account in the Control Ledger.

(5 and 6) **Sales and Bought Ledgers.** As regards the ledgers, these are on exactly the same lines as obtain in any system, and no complication or adjustment is necessary where a system is on a self-balancing basis.

(7) **Cash Book.** In a system where the ledgers are made capable of being balanced separately it will readily be understood that, to enable the full benefit to be reaped, and in order to achieve the desired result with a minimum of clerical labour, the Cash Book cannot be on the usual lines. Indeed, it is in the Cash Book that the usual lines are departed from more than is the case in the ruling of the Day Books, Invoice Books, and other subsidiary books. Bearing in mind that it is necessary to analyse all receipts and payments according to the ledgers to which they are posted, it can readily be understood that, in concerns where many ledgers form part of the system, the analysis required is considerable.

In Form 2 below, a specimen ruling for the receipts side of a Cash Book is set out.

These totals are carried to the General Cash Book and are entered up in the columns applicable. Since the details have been already posted to the Sales Ledger Accounts no further posting of these details is required from the General Cash Book, the entries in the folio column can therefore refer to the Subsidiary Cash Book.

Taking first this side of the Cash Book, where

Form No. 2.

CASH BOOK (RECEIPTS SIDE)

Date.	Particulars.	Ledger Folio.	Dis- counts.	Sales Ledgers.	Bought Ledger.	Imper- sonal Ledger.	Private Ledger.	Sundries.	Total.	Bank.

there are a number of Sales Ledgers it is convenient to have a subsidiary Cash Book containing the record of the cash received from customers in payment of Sales Ledger Accounts. A specimen form of ruling is set out on Form 3.

occasions if desirable, the Cash Book is balanced off and the additions of the analysis columns are made, the cross casts being agreed.

The total of the Impersonal Ledger column is then posted to the credit of the Impersonal Ledger

Form No. 3.

SUBSIDIARY CASH BOOK (SALES LEDGERS RECEIPTS)											
		1.	2.	3.	4.	5.	6.	7.	8.	9.	
Date.	Name of Customer.	Ledger Folio.	Dis-count.	Cash Received	Ledger 1.	Ledger 2.	Ledger 3.	Ledger 4.	Ledger 5.	Daily Discount Total.	Daily Cash Total.

In the first column are entered the discounts allowed to customers, and in the second column the amount of cash received on account of Sales Ledgers Accounts. The details of these two columns are posted by the clerks having charge of the respective ledgers to the credit of the proper accounts. As each clerk posts the items relating to the accounts in the ledger in his charge, he extends the amount of the cash and the discount allowed into the column applicable to his ledger.

The form of ruling allows for five Sales Ledgers. In the eighth column is entered the total discount allowed referring to the cash received each day, and in the ninth column is entered the total of the cash received on account of Sales Ledger each day.

The Subsidiary Cash Book is ruled off periodically, for example, at the end of each month, the totals being dealt with as follows—

The total of the discount column is posted to the debit of the Discounts Account in the Impersonal Ledger, and the totals of the analysis columns (comprising both cash and discount) are posted to the credit of the Control Accounts referring to the various Sales Ledgers in the Control Ledger. The total of the discount column is posted also to the debit of the Impersonal Ledger Control Account in the Control Ledger.

In the General Cash Book the remaining columns are those for receipts which are posted to the credit of accounts in (1) the Bought Ledger ; (2) the Impersonal Ledger ; (3) the Private Ledger. The remaining analysis column is for use in the case of cash contras, or for the purpose of inserting the monthly balance at bank or overdraft, as the case may be.

At the end of each month, or on more frequent

Control Account in the Control Ledger, the total of the Private Ledger column to the credit of the Private Ledger Control Account in the Control Ledger, and the total of the Bought Ledger column to the credit of the Bought Ledger Control Account in the Control Ledger.

The items contained in the "Sundry" column not affecting the ledgers in any way, the total of that column will not require to be dealt with.

In order to minimise the labour of posting, it may be desirable to sub-divide the Impersonal Ledger column or the Private Ledger column into the heads under which items contained in those columns may require to be posted. For instance, under the heading, Imperial Ledger Accounts, it may be desirable to have a column into which are entered such frequent receipts as "Cash Sales" in order that the total of such receipts may be periodically posted so that the labour involved in posting such receipts in detail may be done away with.

Such sub-division in no way interferes with the working of the system so long as it be borne in mind that the total of items so posted to the Impersonal Ledger must be posted also to the Impersonal Ledger Control Account in the Control Ledger.

In cases where considerable sub-division is necessary or desirable, from a labour-saving motive, it is convenient to have a subsidiary Cash Book, ruled as required for each ledger, the daily total of each subsidiary Cash Book being carried to the General Cash Book.

Quite apart from the question of necessity, it is convenient to have such subsidiary Cash Books as a part of the system in order that the posting of each ledger may be proceeded with with a minimum of delay. Where such subsidiary Cash

Books are used, the clerk in charge of any ledger may proceed with the posting of the cash received to his particular ledger without having to wait until the posting to some other ledger has been completed and the value of quick and up-to-date posting cannot be over-estimated, not only from the view of commercial utility, but also when the necessity arises for the drawing of a Trial Balance or the preparation of interim or personal accounts at short notice.

PAYMENTS SIDE OF CASH BOOK. A specimen ruling of the payments side of a Cash Book is set out in Form 4. As in the case of the receipts side of the Cash Book it is necessary to provide columns for the analysis of the payments according to the ledgers to which the payments will be posted. In the example of ruling provided, it is assumed that one Bought Ledger only is in use. Should more than one Bought Ledger be in use further columns should be provided as required.

referring to the particular Sales Ledger in the Control Ledger.

The column provided for payments posted to the Impersonal Ledger should be posted in total to the debit of the Impersonal Ledger Control Account in the Control Ledger.

The remarks applicable to the receipts posted to the Impersonal Ledger apply equally to the details of payments posted to that ledger. In order to effect a saving of labour in posting it is desirable to subdivide this column into such headings as "Salaries and Wages," "General Expenses," "Cash Purchases," etc., and this may be done, either by providing further columns, or by analysing the column itself and writing in the result of the analysis at the foot of the column. Whichever method be adopted the procedure is the same for the self-balancing system.

The column provided for payments posted to the Private Ledger should be posted in total to the

Form No. 4.

CASH BOOK (PAYMENTS SIDE)

Date.	Particulars.	Ledger Folio.	Dis- counts.	Bought Ledger.	Sales Ledgers.	Imper-sonal Ledger.	Private Ledger.	Sun- dries.	Total.	Bank.

In the discount column should be entered the discount allowed by suppliers, and the total of this column should be posted to the credit of the Discounts Account in the Impersonal Ledger in the usual way.

In the Bought Ledger column should be entered the payments to suppliers for goods purchased from them, and the total of this column and the total of the Discounts column together should be posted to the debit of the Bought Ledger Control Account in the Control Ledger. The total of the Discounts column should be posted also to the credit of the Impersonal Ledger Control Accounts in the Control Ledger.

In the Sales Ledger column should be entered payments to customers on the Sales Ledgers. Such payments in ordinary circumstances will be few in number, and will usually be in repayment of overpayments by customers or refunds of the amounts charged for goods returned by them. Since such payments will be few in number it is entirely unnecessary to provide a column for each Sales Ledger. The total of this column should be analysed, and the amount of such analysis should be posted to the debit of the Control Accounts

debit of the Private Ledger Control Account in the Control Ledger.

The remaining analysis column should contain contra items, agreeing with similar entries on the receipts side, and also the amounts of cheques drawn for petty cash. These should be posted in detail to the receipts side of the Petty Cash Book, such amounts not affecting the ledgers until posted from the Petty Cash Book.

(8) **Petty Cash Book.** This book is ruled in the usual way. On the debtor side should appear the column containing the details of cash received agreeing with the items in the sundries column on the payments side of the Cash Book. On the creditor side should appear the total payments column and the usual analysis columns for the purpose of analysing the payments under the various heads of expense. The totals of these columns should be posted in most cases to the Impersonal and Private Ledgers, and also to the debtor side of the Impersonal Ledger Control Account or the Private Ledger Control Account in the Control Ledger. It is unnecessary to post such items separately to the Control Accounts. A summary may be made of the items

posted to each ledger (to the various accounts), and the total only thus arrived at may be posted to the Control Account concerned in the Control Ledger.

In most Petty Cash Books where an analysis of payments is made it is usual to have a "Sundries Column" into which are extended such items as do not come under the heads provided by the separate columns.

This "Sundries Column" is provided with a folio column to enable the items to be posted to their proper accounts independently, and the items in this column will usually require posting to different ledgers. The total of this column, therefore, cannot be posted to any one particular Control Account in the Control Ledger, but will require to be analysed according to the ledgers concerned and a summary entered at the foot of the column.

The details of this summary should be posted to the debtor side of the particular Control Accounts. In addition to the Private and Impersonal Ledgers to which items in this column may be posted, there will usually be found items of payments posted to the Bought Ledger in settlement of small accounts or to the Sales Ledgers in payment of credit balances standing on Sales Ledger accounts for allowances made to customers or returns from them, etc. It must be remembered that, as regards items posted to the Sales Ledger (usually few in number), the analysis must be made according to the various Sales Ledgers concerned, in order that the Control Account of each Sales Ledger in the Control Ledger may be debited.

In some concerns it is the rule to keep the Petty Cash Account in the Impersonal Ledger, to which account the amounts drawn for petty cash are debited. In such cases it must be remembered that the total of such sums must be debited to the Impersonal Ledger Control Account.

The Petty Cash Book in this case is kept only as a memorandum book and the analysis is periodically passed through the Journal, the total of the payments being credited to the Petty Cash Account in the Impersonal Ledger and the details of the analysis going to the debit of the accounts concerned.

Where this method is in use the Control Accounts will be debited or credited in the proper manner from the Transfer Journal as described below.

(9) Bill Books. (a) BILLS RECEIVABLE BOOK.

The usual form of ruling for the Bills Receivable Book will obtain, the Sales Ledger Accounts being credited and the Bills Receivable Account in the Impersonal Ledger being debited with the total as the Bill Book is periodically posted.

The transactions in bills are not usually so numerous as to require separate columns for

the Sales Ledgers in order to arrive at the total amount of bills posted to each Sales Ledger. It will usually suffice to have one common column, the initial letter or number of the ledger to which each item is posted being clearly inserted against each item in the folio column. The items will be analysed according to the ledger to which each is posted, and the totals of such analysis will be posted to the credit of the various Sales Ledgers Control Accounts in the Control Ledger.

The total of the Bills Receivable Book will, as customary, be debited to the Impersonal Ledger Control Account.

In some cases a discount is allowed on payment by bill in the same way as in payment by cash; where such cases are numerous a discount column should be provided in the Bills Receivable Book, the total, besides being posted to the debit of Discounts Account in the Impersonal Ledger, going to the debit of the Impersonal Ledger Control Account in the Control Ledger. The analysis of the details, according to the Sales Ledgers to which they are posted, will be credited to the various Sales Ledger Control Accounts in the Control Ledger.

(b) BILLS PAYABLE BOOK. The form of the Bills Payable Book will be as usually adopted, and where only one Bought Ledger is included in the system of books no variation from the usual form whatsoever will be required. The details will be posted in the usual way to the debit of the Bought Ledger Accounts, the total being posted to the credit of Bills Payable Account in the Impersonal Ledger. To complete the self-balancing system the total will be posted to the debit of the Bought Ledger Control Account and to the credit of the Impersonal Ledger Control Account in the Control Ledger. The same remark as regards discounts applies to the Bills Payable Book as to the Bills Receivable Book, except that the postings will, naturally, be converse.

As regards discounts in the case of Bills Receivable or Payable, where these are not numerous, it is the usual custom to put these through the Journal, the procedure following that described below in order to fulfil the requirements of a system allowing the ledgers to be balanced separately.

(10) Transfer Journal. Transfers are of two kinds—

(1) Transfers from accounts in a ledger to other accounts in the same ledger.

(2) Transfers from accounts in a ledger to accounts in another ledger.

It is obvious that in the case of (1) no entries are necessary through the Transfer Journal since such transfers cannot interfere with any system enabling ledgers to be balanced separately, but

in order to preserve uniformity it is recommended that such transfers be passed through the Journal.

As regards transfers under heading (2), it is necessary to have a record in a convenient form in order that the necessary alterations involved may be adjusted in the Control Accounts, such transfers necessarily affecting the total debits or credits in the ledgers concerned.

A form of Journal is shown in Form 5. (See Inset.)

It will be noticed that the form of Journal departs from the usual form of Journal with two columns, but the suggested form, which is found in practice to be the one most suitable, need not necessarily be adopted. Where, however, the ordinary form of Journal is used it is necessary to analyse each column according to the ledgers to which the items in each column are either debited or credited, and to post the details of the analysis so arrived at to the Control Accounts concerned in the Control Ledger.

In the suggested form of Journal the left-hand side of the Journal is devoted to the entries affecting the debtor sides of the various accounts, and the right-hand side is devoted to the entries affecting the creditor side of the accounts concerned. Each side is analysed, a column being provided for each ledger. In the example shown the following ledgers are allowed for—Impersonal Ledger, Private Ledger, five Sales Ledgers and Bought Ledger.

Examples of entries which would require to be put through the Journal are as follows—

(1) Transfers from one Sales Ledger Account to another Sales Ledger Account where an account has been wrongly debited in the first place from the Day Book.

In such a case the item should be entered in the column on the left-hand side applying to the ledger in which is contained the account to be debited. On the right-hand side the same amount should be entered in the column applying to the ledger in which is contained the account to be credited.

(2) Transfers to put into effect "contras" between Sales Ledgers Accounts and the Bought Ledger Accounts.

In such a case the items should be entered on the left-hand side of the Journal in the column provided for the Bought Ledger, and on the right-hand side in the column provided for the Sales Ledger in which is contained the account to be credited.

(3) Allowances made to customers which cannot properly be put through the Sales Returns Book or the discounts column of the Cash Book in the ordinary way.

In such cases the items will appear in the Impersonal Ledger column (since the Allowances Account is contained in the Impersonal Ledger) on the left-hand side and in the column on the

right-hand side applying to the Sales Ledger in which appears the customer's account concerned.

(4) Allowances made by suppliers which cannot properly be put through the Bought Returns Book or discounts allowed column in the Cash Book.

Such cases will be dealt with in the same manner as (3), but conversely.

(5) Bad debts written off.

Such items will be debited in the Impersonal Ledger to the Bad Debts Account and credited to the accounts concerned in the Sales Ledgers through the Journal, appearing on the left-hand side in the Impersonal Ledger column and on the right-hand side in the column referring to the Sales Ledger in which is contained the account to be credited.

(6) Closing entries and special transfers.

These will be put through, observing the same principle, the item to be debited to the account concerned always being entered in the column applying to the ledger whose total debits will be increased thereby, the same procedure being conversely observed in the case of the credit entries.

It will be appreciated that the Journal cannot be written up in the first place by any one clerk, the persons making the necessary entries being the clerks who have charge of the ledgers concerned in the entries to be put through. In practice each entry is put through completely by one of the clerks whose ledger is concerned by arrangement with the clerk in charge of the other ledger concerned. The entry, so far as it relates to the ledger kept by the other clerk, is checked by him, and he is held responsible that the entry is entered into the correct column and is duly posted to his ledger. Since every clerk in charge of a ledger may be concerned in entries through the Journal it is advisable to make a senior clerk responsible for periodically examining the Journal and requiring explanations for any entries not sufficiently explanatory. In many systems of sectional balancing the Journal is a fruitful source of breakdown, and therefore every care should be taken to have a responsible clerk to supervise its use by the clerks generally.

At the end of every month the additions of the columns on both sides of the Journal are totalled, and in order to complete the self-balancing system the following postings are made—

On the debtor side the total of each column (representing the total debits made to the accounts in the ledger for which such column is provided) is posted to the debtor side of the Control Account concerned in the Control Ledger.

On the creditor side the total of each column is posted, on the same principle, to the creditor side of the Control Account concerned in the Control Ledger.

The foregoing details give particulars of the

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Impersonal Ledger.	Private Ledger.	Bou Led	Sales Ldger 1.	Sales Ldger 2.	Sales Ldger 3.	Sales Ldger 4.	Sales Ldger 5.

manner in which the subsidiary books should be treated in order to fulfil the requirements of a system for self-balancing, and the importance will be understood of the correct analysis of all items according to the ledgers to which the items are posted in order that the corresponding postings in total may be made to the respective control accounts. Should inaccuracy in analysis, addition, or posting of the control figures occur, the re-checking will of necessity involve more time since not only have the ordinary postings, etc., to be re-checked in the usual way, but the control details and totals have also to be re-checked.

Should any difficulty occur in balancing any ledger in the system it is desirable in the first place to re-check the control postings, but a certain and quick check on the Control Accounts themselves is available by ascertaining that the Control Accounts, taken as a whole, balance. If this be the case, then it may be assumed that so far as arithmetical accuracy of the postings and the addition of items is concerned, each Control Account, taken separately, is correct.

Ledgers. It will be observed that in such a system as is described enabling the ledgers to be balanced separately, no deviation from the ordinary form of ledger is necessary, nor can the ledger accounts themselves in any way be altered from the usual form. The installation of such a system, then, involves some adjustment in subsidiary books only, and can therefore be instituted with very little delay or inconvenience in any business where its results are useful.

Control Ledger. As has been already pointed out the Control Ledger is a collection of Control Accounts only, each Control Account being a summary of the ledger to which it relates. If the balances on these accounts are extracted, and the balance on the Cash Book and Petty Cash Book respectively taken into account, the Control Ledger should itself balance, proving the control system as regards additions and the "arithmetical" accuracy of the extensions. It does not, however, prove the accuracy of extensions to the proper columns in subsidiary books, nor that the postings have been made to the proper Control Accounts applicable.

The Control Ledger should, however, be itself proved in this way as the first step in balancing, thus proving the accuracy of additions and numerical accuracy of extension.

The Control Accounts in the Control Ledger will be as follows—

(a) Sales Ledgers Control Accounts (one Control Account for each Sales Ledger).

(b) Bought Ledger Control Account, or if more than one Bought Ledger are in use, a Control Account for each Bought Ledger.

(c) Private Ledger Control Account.

(d) Impersonal Ledger Control Account.

Examining each of the Control Accounts separately—

(a) Each Sales Ledger Control Account contains on the debtor side—

(1) The total of the opening debtor balances on the Ledger.

(2) The totals of the sales posted to the Ledger (from Day Book).

(3) Transfers (from Journal).

(4) Other debits, such as Dishonoured Cheques, Bills Returned and Interest (from the Cash Book or Journal).

(5) Cash (from Cash Book or Petty Cash Book).

As regards (1). The opening balances will be the balance brought down on the Control Account at the time when the books were last balanced if the self-balancing system has been in operation previously. If the system has been installed after the books have been running some time previously, this starting entry will be the total of the schedules of the balances standing on the ledger at the time when the system was put into operation, and such schedules should be referred to.

On the credit side will appear—

(1) The total of the opening Credit balances of the Ledger (usually few in number).

(2) Cash received (from Cash Book).

(3) Discounts (from Cash Book column or from Journal).

(4) Returns (from Sales Returns Book).

(5) Bills Receivable (from Bills Receivable Book).

(6) Bad Debts (from Journal).

(7) Transfers to Sales Ledger Accounts or Transfers from Bought Ledger Accounts (from Journal).

(8) Other credits, such as cheques stopped or special allowances (from Cash Book or Journal).

The balance on the Control Account will represent the total of the debit balances on the ledger (less the credit balances, if any), and when agreed with the schedules of ledger balances, should be brought down and will thus form the starting balance on the Control Account for the next period. The debit balance will be distinguished from the credit balance (if any), the amounts being brought down on the respective sides of the account.

Should the balance on the Control Account not agree with the total of the schedules of ledger balances, the necessary steps can immediately be taken to discover the error.

The first step to be taken is to ascertain whether the Control Account is itself correct. This involves but a very short time. As explained earlier, if the Control Ledger balances, it can be safely assumed that items have been analysed

correctly as regards numerical accuracy, that the postings of the Control Accounts are correct as regards the amounts and that the additions are correct. It is necessary, therefore, to ascertain only whether the totals have been posted to the correct Control Accounts and whether the extension of items in subsidiary books have been made to the proper columns or, in the case of subsidiary books not provided with analysis columns, whether the analysis of the total column has been correctly made. Where other Control Accounts have been agreed with the ledgers which they represent, it will be necessary to check the analysis or posting of items connected with such ledgers. It will be readily understood, therefore, that the checking of the "control" postings can be speedily accomplished.

As soon as the accuracy of the Control Accounts has been established, the discovery of the error connected with the ledger itself may be proceeded with.

With the possibility of an error in mind, it is the custom in some businesses to combine the extraction of ledger balances with a partial analysis of the ledger Accounts, the total of the Debtor items and the total of the Creditor items being taken out on the schedules in addition to the balances of the account as follows—

	Dr.			Cr.			BALANCE.		
	£	s.	d.	£	s.	d.	£	s.	d.
John Smith .	126	4	8	110	2	3	16	2	5

When the schedules are completed the total, therefore, shows, not only the total balances, but also the total of the Debtor entries and the total of the Creditor entries in the Ledger. These amounts should agree with the totals of the Debtor and Creditor sides of the Control Account respectively, and where a difference is found the error may be looked for accordingly.

The preparation of balance schedules in this form involves necessarily a somewhat longer time, but it is found in practice that the extra time is amply compensated for by the saving of labour following on the location of the error either on the debtor side or the creditor side, the checking required being about one-half of that where the error has not been so located.

(b) **Bought Ledger Control Account.** The Bought Ledger Control Account contains on the debtor side—

(1) The total of any debtor balances on the Ledger at the commencement of the period brought down on the last balancing of the books.

(2) Cash paid (from Cash Book or Petty Cash Book).

(3) Discounts (from the Cash Book discounts column or from the Journal).

(4) Bills payable (from the Bills Payable Book).

(5) Returns (from Bought Returns Book).

(6) Other debits such as allowances (from Journal).

(7) Transfers (from Journal).

On the creditor side will appear the following items—

(1) The total of the creditor balances on the ledger at the commencement of the period brought down on the last balancing of the books.

(2) Purchases (from Invoice Book).

(3) Transfers (from Journal).

(4) Other credits such as cheques stopped (from Cash Book), or entries to effect adjustments (from Journal).

The balance on the Bought Ledger Control Account will be the total of the creditor balances on the Bought Ledger (less the debtor balances), and after agreement with the total of the schedules of Bought Ledger balances will be brought down in two amounts as already explained in the case of the Sales Ledgers Control Accounts, but conversely.

In the case of the existence of a difference between the balance on the Bought Ledger Control Account and the total of the balances extracted from the Bought Ledger itself, the same steps should be taken for its discovery as have already been explained in the case of an error existing in the Sales Ledger, the principle being exactly the same. Here again it will be found useful to set out the total of the debtor and creditor sides as well as the balances when extracting the balances from the ledger in order that the side of the ledger on which the error exists may be ascertained.

(c) **Private Ledger Control Account.** The Private Ledger Control Account will show on the debtor side the totals of all items posted to the Dr. side of the Private Ledger Accounts and on the creditor side the totals of all items posted to the Cr. side of the Private Ledger Accounts from all books.

In most businesses the Private Ledger will contain but few accounts. Usually the accounts contained in the Private Ledger may be equally well contained in the Impersonal Ledger, but by reason of the fact that the Impersonal Ledger is open to the inspection of a number of persons for reference or posting purposes, it is desirable to have such a ledger in which are contained the accounts of a private nature, or accounts exhibiting the financial position of an individual or the firm. Such accounts are the Capital Account or Accounts and the Trading Accounts and Profit and Loss Accounts.

In many cases it is the custom also for the periodical balance sheets to be copied into the Private Ledger for the purpose of ready reference. For practical purposes the Private Ledger may

be regarded as an adjunct to the Impersonal Ledger. It will be appreciated, therefore, that the Private Ledger Control Account is a simple one and its agreement with the ledger presents no difficulty.

Impersonal Ledger Control Account. The Impersonal Ledger Control Account is a summary of postings to the Impersonal Ledger. The accounts in the Impersonal Ledger itself are mostly made up of the postings of totals; for example, the Sales Account and the Purchases Account are made up, in most part, of the totals of the Sales Day Books and the Bought Day Book, the Discounts Account is a summary of the totals posted from the Discounts columns in the Cash Book, and many other postings to the ledger are those of totals.

More particularly is this so where the Cash Book used in the business is so analysed that the items to be posted to the Impersonal Ledger are extended into analysis columns provided for the various accounts concerned and posted in total. Examples of columns which may be provided in the Cash Book are, on the Receipts side, "Cash Sales," "Rents Receivable," and other often recurring receipts according to the nature of the business concerned, and on the Payments side, "Wages," "Salaries," "Cash Purchases," "Private Drawings," "Rent, Rates and Taxes," and so on, the totals of such columns being posted periodically instead of in detail.

In some quarters it has been held that, by reason of the fact that the Impersonal Ledger Accounts are made up mostly of totals, the provision of the Impersonal Ledger Control Account is unnecessary and involves an amount of extra clerical work which is not justified.

Where this view is held, it is the custom to have the various Ledger Control Accounts in the Impersonal Ledger regarding it as the Control Ledger containing the summary of every other ledger in the system and therefore capable of being balanced independently of the other ledgers. At first sight this method is desirable in so much as a certain amount of extra posting is thereby saved.

Upon careful examination, however, and in practice, it will be found that this method is not to be recommended. By having a separate Impersonal Ledger Control Account in the Control Ledger, the latter becomes entirely self-contained after bringing into account the balances on the Cash Book and Petty Cash Book. The Impersonal Ledger, by reason of the independent check upon it, can be proved entirely independently and therefore any error which may exist in the Impersonal Ledger may be sought for immediately without waiting for the "proof" of any other ledger. It must be remembered that a considerable number of the postings to the Impersonal Ledger

Accounts consist of items passed through the Journal, which must of necessity be posted in detail and not in total. These items, where an Impersonal Ledger Control Account is kept in the Control Ledger, are posted to the Control Account in total as already explained in the paragraph dealing with the Journal. Other methods may be adopted also to reduce the work of posting to the Impersonal Ledger Control Account. For instance, in place of the posting of each monthly total of the Day Book and the Invoice Book to the debtor or the creditor side of the Impersonal Ledger Control Account respectively, the total may be summarised in these Books at the end of each six months or at the end of each year, and the total only of such summary posted. The same method can obtain also in the case of the Sales Returns Book or of the Bought Returns Book, and thus a considerable amount of "duplicated" posting may be avoided.

Apart from the fact, therefore, that the Control Accounts are not an essential part of the system of book-keeping, and should therefore be contained in a separate book, it will be appreciated that the avoidance of an Impersonal Ledger Control Account is to be deprecated as losing the advantage of an independent check on the Ledger which cannot but prove extremely useful.

It may be mentioned in connection with the Cash Book that it is the rule in some businesses, in order to make the ledgers entirely self-contained, to carry the monthly totals of the Cash Book to a "Bank Account" in the Impersonal or Private Ledger, such account therefore showing the same balance as does the Cash Book from time to time.

More often does this method occur in the case of the Petty Cash Book, which is then regarded solely as a memorandum book as has already been explained in the paragraph touching on this subject.

OTHER METHODS OF BALANCING LEDGERS SEPARATELY.—Although not properly coming under the heading of "Self-Balancing Ledgers," it is convenient to consider the question of balancing ledgers separately where no self-balancing system exists.

It often happens that an error of some sort exists in the books and is disclosed in the trial balance. Where the re-checking of the books fails to ascertain the error, usually arising in such a case by a figure written in such a manner as to cause it to be taken as either of two different figures, it is necessary, for a saving of time and labour, to locate the error in one particular ledger.

In such a case the principle involved is exactly the same as described in the foregoing, that is to say, a Control Account must be raised by a complete analysis of all subsidiary books.

The most convenient manner is to extract the analysis on to a sheet of analysis paper. For

example, in the case of the Sales Day Books, the column containing the details of the debits must be analysed according to the ledgers to which the items are posted.

Where many Sales Ledgers are in use, in the majority of concerns the initial letter of the ledger will be placed against the folio number referring to the ledger in the folio column, and it is therefore a simple matter to extract the items posted to any particular ledger. The details of such analysis will be the debits in respect of sales to the Sales Ledgers Control Accounts. The other totals to be either debited or credited to the Control Accounts will be ascertained in a similar manner, and the Control Account can therefore be written up without any insuperable difficulty so far as the subsidiary books are concerned.

The only figures to be debited or credited to the Control Accounts which cannot be ascertained in this manner are those of transfers from one Sales Ledger Account to another Sales Ledger Account, or transfers between accounts in the Bought Ledger and accounts in the Sales Ledgers. Other transfers which cannot be ascertained from any book of first entry and which will affect the various Control Accounts are those between the Sales Ledgers and the Impersonal Ledger relating, for instance, to bad debts written off and between the Bought Ledger or Ledgers and Impersonal Ledger relating to personal allowances or adjustments, etc.

For the purpose of making up the Control Accounts, transfers between accounts in the same ledger can be disregarded, since the balances on the Control Accounts are not affected.

As regards other transfers, unless it be a rule that these be put through the Journal (in which case the totals affecting each ledger can be easily ascertained by analysis) it is necessary for each ledger to be gone through and for an analysis of such transfers to be made direct from the various ledgers. Such analysis can be readily agreed since the total debit transfer entries in all the ledgers should agree with the total credit entries.

When the total analyses have been extracted the preparation of the Control Accounts is a simple matter, following in principle the method explained previously.

The above method of balancing the ledgers separately may be applied concurrently with the checking of the books.

It is assumed that the checking of postings will be carried out by two persons, one taking the subsidiary book and the other taking the ledgers concerned, the checking of one ledger from such book usually being completed entirely before the entries to another ledger are checked.

The person calling the entries from the subsidiary book, which are to be checked into the ledger, is provided with a sheet of analysis paper

and, simultaneously with the calling of the item, the posting of which is to be checked, he enters the amount of such item in the column provided on the analysis sheet relating to the ledger concerned.

The extra time involved in this process, if any, will not be considerable, and the result will be the preparation of totals from which the Control Accounts can be built up.

The adjustments required by transfers, in this case, will be entered up in the proper analysis columns of the memorandum analysis sheets by the person engaged on the extraction of the ledger balances.

It will be seen from the foregoing that it is possible, even where no adequate system of Self-Balancing Ledgers has been instituted, and the necessary provision of analysis columns allowed for in the subsidiary books or books of first entry, to balance the ledgers used in a system of books separately. The work involved and the possibility of errors must, however, of necessity, in such a case, be greater than is the case where such a system has been carefully provided for and applied, and its advantage realised before the necessity for its application has urgently arisen.

SET-OFF.

A species of defence to an action at law. Whenever a plaintiff puts forward a claim in an action, and the plaintiff is at the same time indebted to the defendant in respect of the claim, the defendant, if he specially pleads it, is enabled to cancel so much of the claim as his own covers. Thus, if A claims £100 against B, and B asserts that £50 of the £100 has been paid off, B can raise the question of this £50 as a set-off, and A's claim is then reduced to £50. If any alleged claim on the part of B has to do with matters which are entirely distinct from those upon which A brings his action, B may make a counter-claim, and herein lies the difference between a set-off and a counter-claim. In fact, whereas a set-off is always connected with the claim of the plaintiff, the counter-claim is, in reality, a new and distinct action.

As to set-off in cases of bankruptcy, see **MUTUAL DEALINGS.**

SETTLEMENT.

(See **VOLUNTARY SETTLEMENT.**)

SETTLEMENTS, MARRIAGE.

(See **MARRIAGE SETTLEMENTS.**)

SHARE CAPITAL.

(See **AUDITING**, p. 87; **BALANCE SHEET**, p. 141; **LIMITED COMPANY ACCOUNTS**, p. 628.)

SHAREHOLDERS AND AUDITORS.

(See **AUDITING**, p. 69.)

SHAREHOLDERS' COMMITTEE, INVESTIGATION ON BEHALF OF.

(See INVESTIGATIONS, p. 585.)

SHAREHOLDERS' INTEREST OUTSTANDING.

(See BALANCE SHEET, p. 138.)

SHAREHOLDERS, REGISTER OF.

(See AUDITING, p. 71.)

SHARE LEDGER.

(See LIMITED COMPANY ACCOUNTS, p. 631;
MEMBERS, REGISTER OF.)

SHARE LEDGER AND BROKER'S LEDGER.

(See FINANCIAL HOUSES AND INVESTORS,
ACCOUNTS FOR, p. 479.)

SHARE WARRANTS TO BEARER.

The issue of share warrants by a company is governed by the provisions of Section 37 of the Companies (Consolidation) Act, 1908, the effect of which is that, if the Articles provide, a share warrant may be issued in lieu of the certificate representing *fully paid* shares. The member whose shares are affected ceases to be a member of the company, and instead of the usual particulars in the register an entry is made of—

- (i) The fact of issue of the warrant;
- (ii) A statement as to shares included in the warrant, distinguishing them by number; and
- (iii) The date of the issue of the warrant.

A warrant so issued is transferable by delivery and gives the holder such rights of membership, if any, as laid down in the Articles, except that his holding will not be qualification for a seat on the board of directors, even although sufficient in amount for the purpose.

Share warrants are issued under the company's seal, and no duty is payable on transfer, as a special duty is paid at the time of issue.

SHARES AS REMUNERATION.

(See AUDITING, p. 77.)

SHARES AT A PREMIUM.

(See AUDITING, p. 78; BALANCE SHEET, p. 142;
PROFIT AND LOSS ACCOUNT, p. 788.)

SHARES, CLASSES OF.

The capital of a limited company is usually divided into shares, the unit of value being of any amount fixed in the Memorandum, or in default, in the Articles. The rights of the holders of shares will depend upon the conditions of issue, and, if no special rights are attached, the shares will be *ordinary* shares of the company. Other

classes of shares may have privileges attached such as are not possessed by the ordinary shareholder.

PREFERENCE SHARES are shares issued to holders who have a preference or priority in respect of dividend, *e.g.* "seven per cent. preference shares" entitling the holder to a seven per cent. dividend in priority to ordinary shareholders. Some preference shares give priority as to repayment of capital on winding up, but this must be specifically provided for. If the conditions of issue do not otherwise provide, the preference shareholders are entitled to receive out of future profits a dividend which has not materialised in any financial year. Such shares are said to be *cumulative* preference shares. Where this right is expressly excluded they are said to be *non-cumulative*. Various classes of preference shares giving varying rights to holders may be issued, provided that the rights of existing shareholders are not interfered with without their consent, such consent being obtained by special resolution of the class concerned. There may be thus 7 per cent. preference shares; 8 per cent. A preference shares of 1921, etc.

DEFERRED SHARES are shares generally issued to persons who have had some interest in the business previous to incorporation. They are sometimes called "founders shares," although these are not necessarily deferred, but may be ordinary shares issued to vendors of property to the company. Deferred shares generally are postponed as to dividend, *e.g.* entitled to the balance of profits after reserves have been adequately provided for and a fixed rate of dividend paid to other shareholders. The auditor has great responsibilities in respect of founders shares as he must protect the interests of the company generally, reporting to the shareholders any attempt to swell the dividends on deferred shares at the expense of adequate provision for contingencies, etc. Particulars of deferred shares must appear in the Prospectus. (See PROSPECTUSES.)

SHARES IN COMPANIES.

(See PROFIT AND LOSS ACCOUNT, p. 788.)

SHARES, TRANSFER OF.

The legal title to shares may be passed from one person to another either by act of law or by act of party. The commonest form of a change of ownership by act of law is by transmission on the death of the owner to his legal personal representative for the benefit of the next of kin or legatees, as the case may be. Change of ownership by act of party is by means of a properly executed transfer, completed by registration in the books of the company.

The form of transfer is governed by the Articles of Association, which may require the formality

of a deed Where Table A applies the following or some form approved by the Board is used—

I, A B of — in consideration of the sum of £— paid to me by C D of — (hereinafter called "the said transferee") do hereby transfer to the said transferee the share (or shares) numbered — in the undertaking called the — Company, Limited, to hold unto the said transferee, his executors, administrators, and assigns, subject to the several conditions on which I held the same at the time of the execution hereof: and I, the said transferee, do hereby agree to take the said share (or shares) subject to the conditions aforesaid. As witness our hands the — day of —.

Witness to the signatures of, etc.

Where no provision is made in the Articles and Table A is excluded, a transfer under hand is sufficient. The obligation to prepare the transfer is in the first case on the transferee, but difficulty seldom arises. The transfer and the share certificate are sent to the company for the purpose of registration. If, however, the holder of shares transfers part only of his holding, he will not allow the transferee to have possession of the certificate, which is the document of title to his shares. In such a case he lodges the certificate with the company, and the secretary certifies on the transfer that the certificate has been lodged. The transfer is returned to the transferee, who completes it by signing and sealing, if necessary, finally returning it to the company for registration. The company prepares two certificates, one for the shares transferred and one for the balance; the former is sent to the transferee, and the latter to the transferor. (See also FINANCIAL HOUSES AND INVESTORS, ACCOUNTS FOR, p. 483; TRANSFERS; TRANSFER OF SHARES, AUDIT OF.)

SHERIFF.

The office of sheriff is undoubtedly one of the most ancient known to the law of England. Originally elective, the appointment has been vested in the Crown since the reign of Edward II, and now it is made annually in a specially constituted Court of the King's Bench Division, consisting of the Chancellor of the Exchequer and a number of the Common Law Judges, which sits "on the morrow of St. Martin's Day," the 11th November. Three landowners of each county are selected from a prepared list, and the final choice of one of the three is made by the King in Council, which is known as "pricking for the sheriff." The appointment is confirmed finally by a warrant signed by the Clerk of the Council.

The sheriff has always been the representative of the central authority of his own county in the execution of the law. He is the returning officer for the Parliamentary divisions of his county; he attends to the collection of the revenue; he waits upon the judges on assize; he summons

the jurors for the assizes; he executes the judgments of the superior courts as to the persons and the property of those within his county; and he is responsible for the execution of criminals. Most of these duties, however, are carried out by the sheriff's subordinates. As the office entails considerable expense, strenuous efforts are made year by year by many persons to avoid the burden of service.

SHERIFF'S COSTS.

(See BANKRUPTCY ACCOUNTS, p. 199.)

SHIP, MORTGAGE OF A.

(See MORTGAGE OF A SHIP.)

SHORT WORKINGS.

(See ROYALTIES.)

SIGHT BILLS.

A bill of exchange or a promissory note must be made payable at a fixed or determinable future time. This time may be calculated in days, weeks, months, etc., but it may also be expressed as "on sight" or "after sight." A bill payable "on sight" is known as a "sight bill," and is the same as a bill payable on demand, that is, it is payable as soon as it is presented to the acceptor. Days of Grace do not attach to sight bills. If a bill is payable so many days after sight, the due date of payment is calculated from the date of presentment for acceptance, and the drawee on accepting should note on the bill the date of his acceptance. (See AFTER SIGHT.)

SIGNATURE ON BILL OF EXCHANGE.

(See BILL OF EXCHANGE, SIGNATURE.)

SIMPLE CONTRACT.

Every contract entered into between parties which is not made by deed is called a simple contract. Such a contract is also known by the name of "parol contract." The assent of the parties to an agreement which is intended to be legally binding, if it is supported by a consideration, is sufficient to constitute a simple contract, and it is immaterial whether it is evidenced by writing or not. In fact, the evidence in writing is only necessary where it is required by statute, e.g. to prove the same in Court. The contract exists all the same, though it may not be enforceable by action, and it is none the less a "parol contract" because there is writing in existence to support it. (See DEED.)

SIMPLICITER.

A Latin word, used to signify simply, directly, immediately, absolutely, or without any circumstances of qualification.

SINGLE ACCOUNT SYSTEM.

Any system of book-keeping the balance sheet

in which shows the capital and liabilities of whatever nature, and the assets of whatever description, on one statement. The term, although also applying to a Single Entry system presenting its final position by means of a statement of affairs, is usually given to accounts kept by Double Entry, and presenting its final position at each balancing by means of a balance sheet in the ordinary form as hereunder.

The title has come into use in contradistinction to what is known as the Double Account System, under which the balance sheet is divided into two parts. The first part shows, on the credit side, the capital and permanent loans raised, and on the debit side the permanent assets on which it has been expended. The balance of this account is carried to the second part or General Balance Sheet, which, of course, also contains the fluctuating liabilities and floating assets. (See also AUDITING, p. 85.)

SINGLE COSTS.

(See COST ACCOUNTS, p. 346.)

SINGLE ENTRY BOOK-KEEPING.

This is a system under which only one entry is made for the majority of the transactions, these being for the purpose of keeping a record of the Personal Accounts. The accounts are written up from the Waste Book entries, the sales being often kept in a separate book, but, if so, the totals of same, although they may be made, are not brought into account. The sales are debited to the Personal Accounts, to which cash is credited from the Cash Book, discounts, etc., inserted, and the account ruled off.

No Purchases Book is kept, but the Ledger Accounts of the creditors are credited direct from the Waste Book, and, on payment, the accounts are debited with cash received, a note made of discounts and allowances, and ruled off.

The Cash Book usually contains only one column on each side, in which both cash and bank items are entered, its balance being a combined cash and bank balance. Although a memorandum of discounts may be inserted in the Cash Book, and a column may be provided for them, the totals of discounts are not brought into account.

In regard to payments for expenses, these simply appear as payments in the Cash Book, no postings being made to Nominal Accounts.

Ledger Accounts are, however, often kept for the purposes of keeping a record of the fixed assets, and introduction of capital.

A trader who keeps his books by this system can only ascertain the position of his affairs at the end of the year by taking out a statement of assets and liabilities, known as a Statement of Affairs, the balance being the capital invested in

the business at that date. The difference between such capital and that at the beginning of the year, with the addition of personal drawings, and the deduction of any capital introduced during the year, is assumed as the profit or loss which has been made.

	£	s.	d.
Capital as per Statement of Affairs—			
31st December, 1921	2,420	2	9
Less Introduced during year	150	0	0
	2,270	2	9
Add Drawings	256	1	4
	2,526	4	1
Less Capital as per Statement of Affairs, 31st December, 1920	2,114	2	11
PROFIT for year	£412	1	2

Single entry accounts sometimes approximate more to double entry, various steps required for a double entry system having been brought into operation, and, in fact, in some cases little is required to complete a double entry system. The name Single Entry is, however, a comprehensive term signifying all systems which are not carried to the finality required in double entry. (See also BRANCH ACCOUNTS, p. 264.)

SINGLE SHIP COMPANIES, AUDIT OF.

(See AUDITING, p. 109.)

SINKING FUND.

It is not easy to define with precision the term "Sinking Fund," which seems to be commonly applied to any fund formed by periodically setting aside and investing money to accumulate at interest. It is clear, however, that the term cannot be properly applied unless there is an existing fund specifically invested and accumulating at interest. The mere retention in hand of sums out of revenue for any purpose does not constitute a Sinking Fund; there must be a specific investment of money intended to accumulate at interest, and for this reason such a term as "Non-accumulating Sinking Fund" should not be used. The object of a Sinking Fund is generally to provide a definite sum of money at a future date by making the smallest possible present provision and depending upon the gradual accumulation of future interest to secure the amount ultimately required. It is commonly used for the purpose of reducing the principal of a national, municipal, or joint stock company debt, or to accumulate a sum of money required at a future date for some other purpose.

HISTORICAL.—With regard to the use of the term "Sinking Fund," Blackstone, in his famous Commentaries, says—

"The surpluses . . . are usually denominated

the Sinking Fund, because originally destined to sink and lower the National Debt." (1765. BLACKSTONE, Comm. I, 329.)

This suggests the origin of the term, and the words also seem to show that even as long ago as the year 1765, when they were written, it had been discovered that the Sinking Fund is by no means infallible. Again, in Lord Byron's *Don Juan* will be found this uncomplimentary reference to the Sinking Fund—

"The Sinking Fund's unfathomable sea . . .
Leaves the debt unsunk, yet sinks all it
receives."

(1824. BYRON, *Don Juan*, Canto, XVI, cxcix.)

The Sinking Fund was first established in the year 1716 by Sir Robert Walpole to be applied to the payment of the principal and interest of the National Debt incurred before the 25th December, 1716. The National Debt at that time did not much exceed £46,000,000. Between 1784 and 1786 the system was established on a great scale by the younger Pitt, who is said to have been misled by the theories of Dr. Richard Price in his work on Annuities, which extols the supposed marvellous virtues inherent to the Sinking Fund. The system was continued until 1813, when Dr. Hamilton proved it to be useless in his *Inquiry on the National Debt*.

Dr. Price, in his writings, inveighs against the sin of interfering with the growth of the Sinking Fund by employing public money allocated to the service of the Sinking Fund to some other purpose. He says—

"By employing the Sinking Fund in bearing current expenses, rather than borrowing new money on new funds, the State, in order to avoid giving simple interest for money, is made to alienate money which must have otherwise been improved at compound interest, and which in time would necessarily have increased to any sum."

And, again, he says—

"Money in a Sinking Fund, if never alienated, is improved, I have shown, at compound interest, but when procured by a loan bears only simple interest. A nation, therefore, when it applies the income of such a fund to current expenses rather than the redemption of its debts chuses to lose the benefit of compound in order to avoid paying simple interest, and the loss in this case is equal to the difference between the increase of money at compound and simple interest."

Dr. Price, then, with some solemnity, gives this terrific illustration of his view. He says—

"The following calculation will show what this difference is. One penny put out at our Saviour's birth to 5 per cent. compound interest would in the year 1791 have increased to a greater sum than would be contained in 300 millions of earths

all solid gold. But if put out to simple interest it would in the same time have amounted to no more than seven shillings and sixpence. All Governments that alienate funds destined for reimbursements chuse to improve money in the last rather than the first of these ways."

It will be seen that, by some extraordinary mental lapse, Dr. Price failed to perceive that the investment of a penny 1,791 years ago at compound interest—which interest, therefore, the investor is not to receive or to touch, but is to allow to accumulate at compound interest during all those centuries, in order that he may at the end of the period receive 300 millions of earths all solid gold—has the same economic result as if the penny were invested 1,791 years ago at simple interest. In the latter case, in each year of the intervening centuries, the investor will have regularly received payment in cash of the annual interest, and could himself invest at compound interest the annual sums so received; by which means, assuming the same rate of interest, he will secure precisely the same results at the end of the time as in the first case, whatever these may be.

The fallacy pervading Mr. Pitt's Sinking Fund may, perhaps, be best explained by a simple example. If the borrower of £100 at 4 per cent. interest lays by £5 a year and invests it in a Sinking Fund in securities yielding 4 per cent. compound interest, the fund will amount to sufficient to pay back the loan in about fifteen years. Assuming, however, the rate of interest to be identical, the borrower might just as well pay the £5 a year, together with an amount equal to the interest on the proportion of the loan redeemed, to the lender in reduction of the loan, for his debt would then be diminishing to precisely the same extent each year as the Sinking Fund to pay it off would be increasing. Indeed, the borrower would be wise to pay the £5 a year, plus an amount equal to the interest saved, off the amount of the debt if, under his contract, he is allowed to do so, because otherwise he will continue responsible to the lender for the full sum during the whole term of the Sinking Fund. Further, he must at the end of the period make good any shrinkage in the market value of the securities in which the Sinking Fund is invested, whereas, if he pays over the money to the lender in reduction of the debt he rids himself of all this needless risk and responsibility.

Or, take the case of a man who, while he has to find money each year to accumulate a Sinking Fund, has also occasion to borrow money either to meet the Sinking Fund instalments or for any other purpose, and finds that his credit is not sufficiently good to enable him to borrow this money except at a rate of interest higher than that which he is able to obtain from the sound and safe securities in which his Sinking Fund is

invested. Such a man will obviously lose money by continuing, on the one hand, the accumulation of a Sinking Fund, while on the other hand he is obliged to borrow more money, and to pay a rate of interest thereon higher than the yield of the Sinking Fund investments. Again, it may happen that a borrower, although able to obtain an original loan at a low rate of interest, may for some reason have to borrow more money during the period of the Sinking Fund, and he may then have to pay a higher rate of interest, say 5 per cent., on the second loan, thereby putting himself in the position of paying 5 per cent. for the use of money which, on the other hand, he is investing for the Sinking Fund at, say, 4 per cent. This was the case with Mr. Pitt's British Sinking Fund, for the more money the Chancellor of the Exchequer wanted, the higher were the terms demanded by the lenders, and, therefore, the money appropriated each year to buy Sinking Fund investments yielding a lower rate of interest, resulted in a recurring and accumulating loss to the nation, for the money used to build up the Sinking Fund might have been more profitably employed for the current requirements of the Exchequer, thereby reducing the need for new loans.

USE OF THE SINKING FUND.—In practice, then, the Sinking Fund is merely a convenient method of accumulating a certain sum of money by a given date by means of annually investing a fixed sum and the interest thereon in the meantime. In the commercial world one of the common uses of the Sinking Fund is to provide for the repayment of capital raised on redeemable debentures and the like. It should be noted that, in such cases, the annual instalment of the Sinking Fund is not a charge against the Profit and Loss Account, but is an allocation of part of the profits earned, and, assuming the profits are properly computed, it will represent the accumulation of a surplus out of undistributed profits. There are several different ways of redeeming debentures with the aid of a so-called Sinking Fund, and the following illustrations are taken from actual cases—

(1) Cumulative Sinking Fund of 2 per cent. per annum, commencing 1st July, 1912, to be applied in purchasing bonds below 110 or in drawings at that figure.

(2) Sinking Fund of £4,250 per annum, to be applied to the purchase of bonds at or below par.

(3) Redeemable at par on 1st January, 1968, by means of a Sinking Fund.

(4) Redeemable at par by half-yearly drawings from a cumulative Sinking Fund of $1\frac{1}{2}$ per cent., or at any time on six months' notice at 105.

(5) Redeemable by annual Sinking Fund of $1\frac{1}{2}$ per cent., or after the 1st July, 1924, on six months' notice, or in the event of voluntary liquidation at 105.

(6) Redeemable at par after twenty-four years

by means of a cumulative Sinking Fund, or earlier on six months' notice.

Although the expression "Sinking Fund" is used in each of the above instances, No. 3 is the only one which relates to a regular Sinking Fund. It will be observed that power is generally taken to enable debentures to be purchased or paid off at short notice, and this is no doubt a wise precaution, having regard to the varying value of money as well as to the great changes which may take place in any business in the course of a few years, and which may possibly improve the security and enable the money to be borrowed at cheaper rates.

Another common use of the Sinking Fund is to accumulate money for the ultimate repayment of Government and municipal loans. The sphere of municipal activity was originally largely confined to making provision for the health and convenience of the public, such as undertaking the supply of water, the making of roads, the building of public offices, markets, cemeteries, etc., and the provision of public parks. None of these are purely profit-seeking or speculative undertakings, and they supply wants common to all living in a municipality. When municipalities first began to borrow for these purposes, it was wisely ordained that some regular annual financial contribution should be provided by the inhabitants of the district out of the rates to enable the necessary loans to be paid off at some definite future date, very often sixty years, which arrangement, of course, enabled the money to be borrowed with ease, and at low rates of interest. Here, then, was the best use, short of the gradual repayment of the loan by annual drawings, for the device known as the "Sinking Fund," and it is doubtless from this that the system has become so familiar.

MISUSE OF THE SINKING FUND.—As time passed, however, it gradually became customary for municipalities to borrow money for other purposes in the nature of trade, such as to provide the necessary capital for the manufacture and sale of such commodities as gas and electricity, or for the provision of tramway undertakings, or other ventures of a trading nature, which had hitherto been carried on by traders working in competition with each other. Such undertakings have always the important characteristic that the commodities and services supplied are not common to the use of all, or necessary to the health and convenience of all. In handling undertakings of this kind, therefore, it became necessary for the first time for municipalities to endeavour to ascertain with accuracy the profit or loss resulting each year from the carrying on of each separate enterprise, in order, amongst other things, to ensure that no part of the cost, which should properly be borne by the users, was cast upon the non-users.

The working cost of carrying on such undertakings includes salaries, wages, rent, coal, fodder, and administrative expenses, all of which are payable year by year in cash, and it also includes expired capital outlay on plant. But, especially in the early days of municipal trading, very little was known about this latter factor of working cost, and in the absence of much knowledge of the matter, it was often claimed by municipalities carrying on trading undertakings, that, provided they repaired and maintained their plant in an efficient working condition, and also set aside each year the amount necessary to build up the Sinking Fund intended to provide for the ultimate repayment of the money borrowed for the plant, they were doing all that could possibly be required. This is not so, however, for the following amongst other reasons—

First, the period of the Sinking Fund was almost always longer than the efficient life of the plant; and, secondly, even if the two periods coincided, the use of the Sinking Fund instalment as the measure of the annual depreciation to be written off plant is unsound. It operates to retard the provision for depreciation, and so to curtail the proper charge against revenue, in the earlier years of the life of the plant, and to accelerate this in later years, by appropriating in advance, in the name of interest, in reduction of the proper provision, sums on account of the income expected to be earned from the use of the plant in future years.

The statement on page 863, headed "Plant Account," will serve to illustrate this.

This statement purports to show the gradual writing off year by year of plant which cost, when new, £6,000, and which has an efficient life of ten years, by the end of which time it will be valueless; for in order to simplify the argument it is assumed there will be no residual value. The statement deals with the Annuity method of providing depreciation, as well as with the Sinking Fund method; but first it will be well to look only at the columns indicated by the letters C, E, and F, which contain the figures relating to the Sinking Fund method.

The Sinking Fund in this case is accumulated at an assumed interest of 3 per cent. per annum, and it will be seen on reference to the foot of Column F that the total interest accruing on the Sinking Fund investments during the ten years amounts to £766. The annual Sinking Fund instalment is between £523 and £524, amounting, if the instalments be added together for the ten years, to £5,234, and if to this sum be added £766, the total interest expected to accrue on the investments over the whole period, the result is the sum of £6,000 at the end of the term, which is the amount required. But, in order to secure this, there has been appropriated in advance,

under the name of interest, one-tenth of £766, or £77, in the first year of the life of the plant to reduce the depreciation provision of the first year from £600 to £523. In the second year there has again been appropriated in advance £77 as interest for that year, whereas only £15 of interest is earned, so that there is an effective allocation for depreciation of £539 only (consisting of Sinking Fund instalment £524 and interest earned £15), instead of £600. In the same way, in the third year the effective depreciation provision will be seen, on reference to Column E, to be £555 (viz., £32 + £523), instead of £600, caused by the fact that, while £77 of interest is appropriated as belonging to the year in fixing the Sinking Fund instalment, only £32 of interest is earned in the year on the money released and invested up to that date.

Now, when money is invested in plant it is from the use of the plant alone that a return can arise, and no part of this must be foretalled. There is no interest. Considerations of interest disappear as effectively as if the money was locked in a box. One cannot talk of interest in connection with plant, but only in connection with money or its equivalent.

And thus, if the annual instalments of a Sinking Fund, running during the estimated life of plant, together with the annual interest earned thereon, are used to measure depreciation, the unexpired value of the plant remains overstated in the books of the undertaking at all periods within the life of the plant. It is not until the end of the period, when the value expires altogether, that the amount in the Sinking Fund reaches the amount of the expired capital outlay (depreciation), which depreciation, according to the common commercial view, accrues equally over the efficient life of the plant, in return for approximately equal annual service. It will be observed on reference to Column C in the statement, that at the end of the fifth year the surviving value of the plant appears as £3,222, whereas, half the efficient life of the plant having expired, the unexpired value is, in fact, £3,000 only.

A study of the effect of using the annual instalments of a Sinking Fund as a measure of annual depreciation would not be complete without an examination of the effect of the use of the Annuity method of providing for depreciation of plant, and on reference to the columns A, B, and D, in the above statement, it will be seen that these show the gradual writing off of the cost of the plant under the Annuity method. In the Annuity method, interest is added, on the one hand, to the capital remaining at the end of each year invested in the plant; and, on the other hand, there is deducted each year an equal annual amount, known as an annuity, sufficient to extinguish the balance of capital outlay, together with the interest additions, by the end of the life period.

PLANT ACCOUNT

Cost, £6,000.

EFFICIENT LIFE, 10 YEARS.

RESIDUAL VALUE, NIL.

		Annuity method of providing depreciation.		Sinking Fund method of providing depreciation.			Annuity method of providing depreciation.	Sinking Fund method of providing depreciation.	
		A.	B. Interest.	C.			D.	E.	F. Interest.
1st year					1st year				
Jan. 1	Original value or cost . .	£ 6,000	£	£ 6,000	Dec. 31	1st Annuity	£ 703	£	
Dec. 31	Interest at 3% on £6,000 . .	180	180		"	Sinking Fund Interest—			
					"	1st Sinking Fund Instalment			
					"	Balance	5,477	523	
								5,477	
		£6,180		£6,000			£6,180	£6,000	
2nd year					2nd year				
Jan. 1	Balance, surviving value . .	5,477		5,477	Dec. 31	2nd Annuity	704		
Dec. 31	Interest at 3% on £5,477 . .	165	165		"	Sinking Fund Interest at 3% on £523		15	
					"	2nd Sinking Fund Instalment		524	
					"	Balance	4,938	4,938	
		£5,642		£5,477			£5,642	£5,477	
3rd year					3rd year				
Jan. 1	Balance, surviving value . .	4,938		4,938	Dec. 31	3rd Annuity	703		
Dec. 31	Interest at 3% on £4,938 . .	148	148		"	Sinking Fund Interest at 3% on £1,062		32	
					"	3rd Sinking Fund Instalment		523	
					"	Balance	4,383	4,383	
		£5,086		£4,938			£5,086	£4,938	
4th year					4th year				
Jan. 1	Balance, surviving value . .	4,383		4,383	Dec. 31	4th Annuity	704		
Dec. 31	Interest at 3% on £4,383 . .	132	132		"	Sinking Fund Interest at 3% on £1,617		48	
					"	4th Sinking Fund Instalment		524	
					"	Balance	3,811	3,811	
		£4,515		£4,383			£4,515	£4,383	
5th year					5th year				
Jan. 1	Balance, surviving value . .	3,811		3,811	Dec. 31	5th Annuity	703		
Dec. 31	Interest at 3% on £3,811 . .	114	114		"	Sinking Fund Interest at 3% on £2,189		66	
					"	5th Sinking Fund Instalment		523	
					"	Balance	3,222	3,222	
		£3,925		£3,811			£3,925	£3,811	
6th year					6th year				
Jan. 1	Balance, surviving value . .	3,222		3,222	Dec. 31	6th Annuity	703		
Dec. 31	Interest at 3% on £3,222 . .	96	96		"	Sinking Fund Interest at 3% on £2,778		84	
					"	6th Sinking Fund Instalment		523	
					"	Balance	2,615	2,615	
		£3,318		£3,222			£3,318	£3,222	
7th year					7th year				
Jan. 1	Balance, surviving value . .	2,615		2,615	Dec. 31	7th Annuity	704		
Dec. 31	Interest at 3% on £2,615 . .	79	79		"	Sinking Fund Interest at 3% on £3,385		101	
					"	7th Sinking Fund Instalment		524	
					"	Balance	1,990	1,990	
		£2,694		£2,615			£2,694	£2,615	
8th year					8th year				
Jan. 1	Balance, surviving value . .	1,990		1,990	Dec. 31	8th Annuity	703		
Dec. 31	Interest at 3% on £1,990 . .	59	59		"	Sinking Fund Interest at 3% on £4,010		121	
					"	8th Sinking Fund Instalment		523	
					"	Balance	1,346	1,346	
		£2,049		£1,990			£2,049	£1,990	
9th year					9th year				
Jan. 1	Balance, surviving value . .	1,346		1,346	Dec. 31	9th Annuity	703		
Dec. 31	Interest at 3% on £1,346 . .	40	40		"	Sinking Fund Interest at 3% on £4,654		140	
					"	9th Sinking Fund Instalment		523	
					"	Balance	683	683	
		£1,386		£1,346			£1,386	£1,346	
10th year					10th year				
Jan. 1	Balance, surviving value . .	683		683	Dec. 31	10th Annuity	704		
Dec. 31	Interest at 3% on £683 . .	21	21		"	Sinking Fund Interest at 3% on £5,317		159	
					"	10th Sinking Fund Instalment		524	
					"	Balance	nil	nil	
		£704	£1,034	£683			£704	£683	£766

Column B shows that the total interest added during the ten years on the capital remaining from time to time invested in the plant, amounts, in this case, to £1,034; and on looking at Column D it will be seen that the annuity amounts to £703, made up of one-tenth of £6,000, or £600, plus one-tenth of £1,034, or £103—together £703. A study of the statement will show why the surviving value of the plant, standing in the books at the end of any year, is the same whether the cost of the plant be written off by the Annuity or by the Sinking Fund method. Another important point is to observe that the difference between the Annuity £703 and the Sinking Fund instalment £523 is £180, and is equal to one year's interest at 3 per cent. on £6,000, the amount of capital involved in this supposed transaction. The reason, shortly stated, is that the Annuity method charges interest on the capital remaining locked up from time to time in the plant, and the Sinking Fund method allows interest on the capital released from time to time; the difference between the two, therefore, being equal to simple interest on the capital sum involved.

AN ELEMENT IN THE VALUE OF GOODWILL.—The opponents of the equal annual instalment, or straight line, method of measuring the annual depreciation of plant, should not overlook the fact, demonstrated above, that the Annuity and Sinking Fund methods of providing depreciation are both based upon what is known as the straight line principle, for in each case the equal annual instalment is taken as the root, and then manipulated by appropriating in advance, in the name of interest, sums on account of income expected to be earned from the use of the plant in future years, thus confusing the surviving value of the plant with what is really an element of value appertaining to any goodwill which may attach to the undertaking.

It may be thought that in the case of the plant shown in the statement the value at the end of the fifth year is, in fact, nearer to £3,222 than £3,000, because during the earlier years of the life of the plant more capital has been locked up in the plant than will be the case during the later years, but it must be remembered that the question under consideration is the value of plant and not the value of the undertaking using the plant. If it is a question of determining the value of an undertaking (as distinguished from the value of plant) for the purpose of sale and transfer from one undertaker to another, the fact that a larger amount of capital has been locked up in plant during the seller's part of the period than during the buyer's part, may be good ground for claiming the payment of a sum for goodwill, but it does not add to the value of the plant. Goodwill is the present value of super-profits (see article on **GOODWILL**) expected to arise in future years out

of the presently existing condition and state of development of an undertaking, the term "super-profits" meaning profits likely to be earned in excess of those required to attract and retain the necessary capital and ability to carry on the enterprise successfully in future. Now, a common condition of plant such as that referred to above, to the extent that it may tend to add to the future profits arising out of the undertaking (because the annual advantage derivable from the use of the plant is much the same, while the capital locked up therein will be less), tends also to add to the present value (if any) of the goodwill of the undertaking; but such existing value is marketable only as part of any goodwill, if and when a purchaser comes along. As the value of goodwill is properly omitted from the financial books of an undertaking unless and until it is actually sold and bought, it is not desirable to appropriate this element of value as a reason for upholding the book value of plant at a sum greater than its true surviving value to a going concern.

In actual practice the effect on the goodwill of an undertaking of the more or the less capital which may at any given time be invested in any particular part of the plant, is usually nullified by the operation of the law of average, because a plant in use generally consists of many classes of plant, and each of those classes comprises units of plant of all ages, so that the part of the plant in the early stages of its efficient life containing the more capital, will be counterbalanced by the part of the plant in the later stages of its efficient life containing the less capital. Thus, it will be found that that part of the capital of an undertaking which is invested in plant remains, as to its bulk, always permanently invested in plant, the units of which are continually passing out of service and being renewed, in the same way as other portions of the capital of an industrial undertaking remain permanently invested in such assets as stock and debts, the constituent items of which are always changing, while the amount of capital which they represent remains a fairly constant sum. The profit earned by the undertaking year by year is itself the full interest or increment accruing to the capital invested, and it is as unsound to forestall and apply future interest (as is involved by the use of the Sinking Fund) in a manner which operates to retain the surviving value of plant in the books at too large a sum, as it would be to apply interest to add to the value of unsold stock or unpaid debts in which a large part of the capital of industrial undertakings is locked up, and for this reason it is a misuse of the Sinking Fund to apply it as the measure of the annual depreciation of plant.

OBJECTIONS TO THE USE OF THE ORDINARY SINKING FUND.—The legitimate

use, then, of the ordinary Sinking Fund is to provide for the redemption *en bloc* of Government or municipal loans, or of loans contracted by profit-seeking undertakings, which are repayable at the end of a stated term of years. But there are serious objections to the use of the ordinary Sinking Fund, arising principally out of the fact that the method involves the retention of investments in hand at the borrower's risk over long periods of years. After briefly considering the objections to the ordinary or "Retained Sinking Fund" method of providing for the redemption of debt, reference will be made to the system of redeeming debt by a modification of the Annuity principle, which may conveniently be described as the "Distributed Sinking Fund" method.

One objection to the Ordinary Sinking Fund method is the absence of security that its provisions will be carried out over the whole period, usually varying from ten to sixty years, and sometimes even extending to eighty years. During all that time economic conditions are liable to change, as a consequence of which not only may the future annual instalments be varied or the money diverted to other more pressing purposes, but the amount already accumulated in the Fund itself may even be alienated and applied to something else for reasons which may then appear adequate. This objection would be remedied by the substitution of the Distributed Sinking Fund method, under which the amount of the annual provision is used for paying off part of the debt, that is to say, it is invested by purchasing the loan itself without further risk, instead of being invested and accumulated in other loans at the continuing risk and responsibility of the borrower.

Other objections to the ordinary Sinking Fund method include the probability that during the period of the Sinking Fund the investments representing the fund will fluctuate and may depreciate heavily in value. Further, the operation of repaying a large loan *en bloc* at maturity involves the selling out of amounts of securities which, even under normal conditions, may be sufficient to depress the market, and possibly, in unfavourable circumstances, may dislocate it altogether.

Again, the ordinary Sinking Fund method involves the use of a schedule containing calculations, at an assumed rate of interest, showing the amount which ought to be in the Sinking Fund at the end of each year of the period. This needs constant watching, as the investments may not realise the rate of interest estimated, and other changes may take place which may necessitate the re-adjustment of the amount of the Sinking Fund instalment.

The view is widely held that investors object to their securities being subject to the possibility of early repayment, and the ordinary Annuity

method of gradual repayment is doubtless unsuitable for the redemption of large loans, involving as it does the payment to each lender, in reduction of his particular holding, of an equal annual sum, or annuity, which includes both principal and interest. But security is the consideration which weighs most heavily with investors, and if they receive their interest regularly, they are not likely to object to the possibility of bonds being repaid at par under a system which operates automatically to steady and maintain the market prices of the bonds.

"DISTRIBUTED SINKING FUND" METHOD.—The "Distributed Sinking Fund" method of repayment is the Annuity principle suitably modified, and it may conveniently be thus described, because an amount equal to the annual Sinking Fund instalment plus the amount of interest saved on the bonds previously repaid is, each year, repaid to lenders holding bonds which are drawn for repayment up to that amount, instead of the instalment being retained and invested in other securities, as is the case with the ordinary or "Retained Sinking Fund" method. This method of gradual repayment of capital is particularly suitable for application to undertakings with capital sunk in wasting assets such as natural raw material, including coal, minerals, nitrate, oil, or in concessions, patent rights and goodwill. On the other hand, capital sunk in industrial plant of all kinds will generally be required again to pay for renewing the industrial plant, and so must not be repaid by instalments, but should be accumulated and retained in hand until required. To illustrate the effect of this gradual repayment of a loan by annual drawings of bonds equal to the required Sinking Fund instalment plus an amount equal to the annual interest on the bonds already redeemed, the case may be taken of a loan of £100,000 at 4 per cent. which, under the terms of issue, is to be wholly repaid in this manner by the end of twenty years. The figures are shown in the table on page 866.

It will be seen by reference to the above table that this method of repayment involves an equal annual charge over the whole period, adding the annual payments of principal and interest together, because, as the interest paid each year on the balance of the outstanding loan decreases, so does the amount equal to the annual interest on the proportion of the loan redeemed increase, and this latter is added to the equal annual amount of the ordinary Sinking Fund instalment, the resulting sum being applied in repayment of part of the outstanding balance of the loan by annual drawings. In suitable cases this method of repayment of a loan has advantages over either the ordinary Sinking Fund method or that which is known as the Equal Annual Instalment method.

TABLE SHOWING "DISTRIBUTED SINKING FUND" METHOD OF ANNUAL REPAYMENT (BY DRAWINGS) OF A LOAN OF £100,000 AT 4 % INTEREST FOR 20 YEARS

YEAR.	REPAYMENT OF PRINCIPAL.			Balance of Loan Outstanding.	Annual Interest Payable.	Total Annual Repayment and Annual Interest.
	Ordinary Sinking Fund Instalment.	Amount equal to Interest on Proportion of Loan Redeemed.	Total Annual Repayment. By Drawings.			
1	£ 3,358.2	£ —	£ 3,358.2	£ 100,000	£ 4,000	£ 7,358.2
2	3,358.2	134.3	3,492.5	96,641.8	3,865.7	7,358.2
3	3,358.2	274	3,632.2	93,149.3	3,726	7,358.2
4	3,358.2	419.3	3,777.5	89,517.1	3,580.7	7,358.2
5	3,358.2	570.4	3,928.6	85,739.6	3,429.6	7,358.2
6	3,358.2	727.5	4,085.7	81,811	3,272.5	7,358.2
7	3,358.2	891	4,249.2	77,725.3	3,109	7,358.2
8	3,358.2	1,060.9	4,419.1	73,476.1	2,939.1	7,358.2
9	3,358.2	1,237.7	4,595.9	69,057	2,762.3	7,358.2
10	3,358.2	1,421.5	4,779.7	64,461.1	2,578.5	7,358.2
11	3,358.2	1,612.7	4,970.9	59,581.4	2,387.3	7,358.2
12	3,358.2	1,811.5	5,169.7	54,710.5	2,188.5	7,358.2
13	3,358.2	2,018.3	5,376.5	49,540.8	1,981.7	7,358.2
14	3,358.2	2,233.4	5,591.6	44,164.3	1,766.6	7,358.2
15	3,358.2	2,457.1	5,815.3	38,572.7	1,542.9	7,358.2
16	3,358.2	2,689.7	6,047.9	32,757.4	1,310.3	7,358.2
17	3,358.2	2,931.6	6,289.8	26,709.5	1,068.4	7,358.2
18	3,358.2	3,183.2	6,541.4	20,419.7	816.8	7,358.2
19	3,358.2	3,444.9	6,803.1	13,878.3	555.1	7,358.2
20	3,358.2	3,717	7,075.2	7,075.2	283	7,358.2
	£67,164	32,836	100,000		47,164	147,164

COMPARISON BETWEEN RESULTS OF ORDINARY OR RETAINED SINKING FUND METHOD AND EQUAL ANNUAL INSTALMENT METHOD.—In order to be able to compare the results of the ordinary or Retained Sinking Fund method with the results of the Equal Annual Instalment method, the table shown on page 867 will be useful. This table relates to a similar loan of £100,000 at 4 per cent. interest extending over a period of twenty years.

As an aid to the study of the subject, columns of figures headed "Increase" are included in the table showing the annual increase at 4 per cent. compound interest which would accrue during the period in the hands of the lenders on the annual sums received by them from the borrowers, in respect of both principal and interest. Thus, under the Sinking Fund method the lenders receive from the borrowers during the period a sum of £4,000 per annum for interest, and the increase (that is to say, the interest earnable) on these annual payments if invested by the lenders at 4 per cent. compound interest during the twenty

years, amounts to £39,112. Under the Equal Annual Instalment method, the like increase on the £5,000 per annum paid to the lenders by the borrowers in reduction of the principal, if invested at 4 per cent. compound interest, amounts to £48,890.4, and on the annually diminishing interest payments to £28,221.6.

It will be seen from the table that a twenty years' 4 per cent. ordinary Sinking Fund to repay a 4 per cent. loan of £100,000 involves the actual payment by the borrowers during the period of £147,164, consisting of £67,164 for the annual instalments (£3,358.2 × 20) and £80,000 for the annual interest (£4,000 × 20), whereas the repayment of the loan by equal annual instalments involves the payment by the borrowers of £142,000, consisting of £100,000 for the annual instalments (£5,000 × 20) and £42,000 for the reducing annual interest, the first annual payment being £4,000 and the last annual payment £200. Thus, £147,164 in cash must be found during the period for the Sinking Fund instalments and loan interest, while only £142,000 is required for the annual repayments and loan interest. This

LOAN £100,000 AT 4 PER CENT. INTEREST FOR 20 YEARS

	ORDINARY OR RETAINED SINKING FUND.					EQUAL ANNUAL INSTALMENT.				
Year.	Capital.		Interest.		Total.	Capital.		Interest.		Total.
	Instalment.	Interest invested.	Paid to lenders.	Increase.		Paid to lenders.	Increase.	Paid to lenders.	Increase.	
	£	£	£	£	£	£	£	£	£	£
1	3,358.2	—	4,000	—	7,358.2	5,000	—	4,000	—	9,000
2	3,358.2	134.3	4,000	160	7,652.5	5,000	200	3,800	160	9,160
3	3,358.2	274	4,000	326.4	7,958.6	5,000	408	3,600	318.4	9,326.4
4	3,358.2	419.3	4,000	499.4	8,276.9	5,000	624.4	3,400	475	9,499.4
5	3,358.2	570.4	4,000	679.4	8,608	5,000	849.4	3,200	630	9,679.4
6	3,358.2	727.5	4,000	866.6	8,952.3	5,000	1,083.3	3,000	783.2	9,866.5
7	3,358.2	891	4,000	1,061.3	9,310.5	5,000	1,326.6	2,800	935	10,061.6
8	3,358.2	1,060.9	4,000	1,263.7	9,682.8	5,000	1,579.6	2,600	1,084	10,263.6
9	3,358.2	1,237.7	4,000	1,474.2	10,070.1	5,000	1,842.8	2,400	1,231	10,473.8
10	3,358.2	1,421.5	4,000	1,693.2	10,472.9	5,000	2,116.5	2,200	1,377	10,693.5
11	3,358.2	1,612.7	4,000	1,921	10,891.9	5,000	2,401.2	2,000	1,520	10,921.2
12	3,358.2	1,811.5	4,000	2,157.8	11,327.5	5,000	2,697.3	1,800	1,661	11,158.3
13	3,358.2	2,018.3	4,000	2,404.1	11,780.6	5,000	3,005.2	1,600	1,799	11,404.2
14	3,358.2	2,233.4	4,000	2,660.3	12,251.9	5,000	3,325.3	1,400	1,935	11,660.3
15	3,358.2	2,457.1	4,000	2,926.7	12,742	5,000	3,658.4	1,200	2,068	11,926.4
16	3,358.2	2,689.7	4,000	3,203.7	13,251.6	5,000	4,004.7	1,000	2,199	12,203.7
17	3,358.2	2,931.6	4,000	3,491.9	13,781.7	5,000	4,364.9	800	2,327	12,491.9
18	3,358.2	3,183.2	4,000	3,791.6	14,333	5,000	4,739.5	600	2,452	12,791.5
19	3,358.2	3,444.9	4,000	4,103.3	14,906.4	5,000	5,129.1	400	2,574	13,103.1
20	3,358.2	3,717	4,000	4,427.4	15,502.6	5,000	5,534.2	200	2,693	13,427.2
	£67,164	32,836	80,000	39,112	219,112	100,000	48,890.4	42,000	28,221.6	219,112

difference of £5,164 is accounted for in the following manner—

Interest at 4% compounded yearly on the equal annual instalments invested for the Sinking Fund, £32,836, and on the loan interest paid £39,112, amounting together to	£
Interest at 4% compounded yearly on the annual sums repaid, £48,890.4, and on the loan interest paid, £28,221.6, amounting together to	71,948
	77,112

The reason of the difference is that the annual payments involved by the Sinking Fund method, although the sum of these is larger, fall in such a way over the period of twenty years that, if invested, they will produce less interest than will the equal annual repayments under the other method plus the loan interest paid, although the sum of these is less. In the latter case, the equal annual repayments plus the loan interest paid represent larger sums in the earlier years and smaller sums in the later years, and, therefore, if invested at 4 per cent., produce £5,164 more interest. The whole economic results of both methods are equal and produce in each case £219,112, being the amount of £100,000 at the end of twenty years if invested at 4 per cent. per annum compound interest. (See also BALANCE SHEET, p. 143; DEPRECIATION, p. 402.)

SINKING FUND CALCULATIONS.

The term Sinking Fund is of somewhat varied application, and primarily suggests the periodical payment or investment of a specific sum or specific sums of money which, under the influence of interest, will accomplish the object sought to be attained. The interest, however, need not necessarily follow the capital nor need the instalments be equal or otherwise in regard to amount and time of payment to acquire the promiscuous appellation of sinking fund though these are general characteristics of many such funds.

Sinking Funds are created for the purpose of making provision for particular assets of declining value, and other descriptions of expenditure, redemption of loans, and the like.

For the redemption of loans we have—

1. Equal periodical instalment or deferred payment system.

2. Annuity or hire purchase system.

3. Accumulative sinking fund.

4. Non-accumulative or non-cumulative sinking fund, which are applicable to the redemption of loan debts of corporations and local authorities, and some of them to Government transactions and to commercial undertakings.

In case 1 there is really no sinking fund. The lender is repaid periodically an equal proportion

of the sum lent with a varying amount of interest at the agreed rate on the principal or capital outstanding from time to time, the amount of interest decreasing with the decrease in the amount of the loan in force.

2. In this instance an equal periodical payment is made to the lender (which comprises both principal and interest) until the loan is extinguished, the characteristics of this mode of redemption or amortisation being that although the lender receives the same amount at each due date of repayment it comprises an increasing amount of principal with a decreasing amount of interest. For instance, let us assume a loan of £50 repayable in five years with interest at 5 per cent. There are several methods of computing the amount of the instalment, among them the following—

(a) the amount of £1 in five years at 5 per cent. is $1.2763 \times 50 = £63.8150$. The amount of £1 per annum in five years at 5 per cent. is £5.5256,

and $\frac{63.8150}{5.5256} = 11.5489$, the annual instalment

required to pay the principal and interest.

(b) The present value of £1 per annum for five years at 5 per cent. = 4.3205, and $\frac{50}{4.3205}$

£11.5489.

Briefly the table is—

Years.	Interest.	Principal.	Amount paid to lender.
	£	£	£
1	2.5	9.04	= 11.54
2	2.04	9.50	= 11.54
3	1.57	9.97	= 11.54
4	1.07	10.47	= 11.54
5	.55	10.99	= 11.54
	<u>£7.73</u>	<u>£49.97</u>	= <u>£57.70</u>

Under the accumulative sinking fund method the lender receives his repayment of the loan at the end of the term, he, in the meantime, being paid interest on the full amount of the loan. The interest on the loan and the interest yielded by the sinking fund are two distinct factors.

Let us assume the repayment of a 5 per cent. loan of £50 in five years with a sinking fund at 3 per cent. Here the sinking fund calculation is as below.

The amount of £1 per annum in 5 years at 3 per cent. is 5.30914, and $\frac{50}{5.30914} = 9.4177$, etc., the annual instalment to be invested to produce at 3 per cent. in 5 years, £50. Then—

Amount of Sinking Fund instalment (say).	£ 9.42
Annual Interest on loan	2.50

Annual sum required to pay the Interest on the loan and to repay the principal 11.92

The Sinking Fund table is—

Annual Instalment to Sinking Fund.	Interest yielded by the Sinking Fund.	
£	£	
9.417		
9.417	.282	
9.417	.573	
9.417	.873	
9.417	1.182	
<u>47.085</u>	<u>2.910</u>	= say £50.

As a variation, what is the present value of an annuity certain of £1 for 3 years to pay 5 per cent. upon the investment, the sinking fund being calculated at the rate of, say, 4 per cent.?

The amount of £1 per annum for 3 years at 4 per cent. = 3.1216. The purchase money is therefore 2.7001, i.e.—

$$\frac{3.1216}{1.05 \times 3.1216}$$

The sinking fund instalment will be—

$$1 - \frac{.05 \times 3.1216}{1.05 \times 3.1216}, \text{ or } \frac{1}{1.05} \times 3.1216 = .864993;$$

which invested yearly at 4 per cent. will amount to 2.7001.

The purchaser or annuitant receives annually = 1.
He pays to the Sinking Fund

.864993

and 5% on the purchase money: £27.001 = .13507

The accumulative sinking fund mode is frequently applied to the redemption of debentures. Let us suppose £10,000 in 5 per cent. debenture stock redeemable at par in 5 years.

The amount of £1 in 5 years at 5 per cent. is 1.27628, and the amount of £1 per annum in 5 years at 5 per cent. is 5.52563. Then the former divided by the latter = .2309745 $\times 10,000 = £2309.745$.

	£	s.	d.
The annual sum required to pay off £10,000 in 5 years with interest at 5% is.	2,309	14	11
The interest at 5% on £10,000 for 1 year is	500	0	0

Fixed sum to be paid to the trustees, which is to be increased by the interest in the redeemed debenture stock. £1,809 14 11

It is necessary only to give the first and second year's working—

	£	s.	d.
Amount of Debenture Stock.	10,000	0	0
At end of first year's payment to trustees	1,809	14	11
	<u>8,190</u>	<u>5</u>	<u>1</u>
	<u>£1,900</u>	<u>4</u>	<u>8</u>

At end of second year's payment to trustees, which should be composed as under—

	£	s.	d.
Fixed sum	1,809	14	11
Interest for 1 year at 5% on £10,000	500	0	0
Less interest payable on £8,190 5s. 1d. at 5%	409	10	3
		90	9 9
	£1,900	4	8

and in like manner for the remainder of the term. At the end of the fifth year the sum payable to the trustees will be found to be £2,199 15s. 4d., which extinguishes the balance outstanding on the Debenture Stock Account.

One of the usual methods of ascertaining the yield of a redeemable fixed term security is by interpolation of the differences between the assumption of two rates, one being a little less and the other a little more than the true rate, or it may be ascertained on the basis of the yield of the sinking fund. It is obvious that when the rate assumed for the sinking fund is the same as the true rate of interest yielded by the security, the sinking fund method and that of ascertaining the true rate are identical. For instance, the true yield of a 6 per cent. bond for £100 purchased for £110 and redeemable in 10 years at par is 4.722 per cent., which may be readily computed.

Let us take 4.722 as the sinking fund rate, and we have—

Annual interest receivable	6	£
Less amount to be annually invested in the Sinking Fund at 4.722% to redeem the £10 (i.e. the difference between the price of purchase £110 and the capital sum receivable at the end of 10 years, viz., £100)	-80542	
	£5.19457	

$$\text{Then } \frac{5.19457 \times 100}{110} = 4.722\% \text{ the true yield.}$$

The book-keeping entries may be framed as under—

Dr. Bond Account and *Cr.* Cash with purchase price.

Dr. Cash and *Cr.* Bond Account with the amount received on redemption.

Dr. Cash and *Cr.* Interest Account with interest received on the bond.

Dr. Profit and Loss Account and *Cr.* Bond Account with the Sinking Fund instalment, £.80542 as above.

Dr. Interest Account and *Cr.* Bond Account with the interest yielded by the Sinking Fund.

Transfer the balance of the Interest Account to revenue.

At the end of the tenth year, the Bond Account would be as under, assuming the bond to have been redeemed—

BOND ACCOUNT

	£		£
Cash	110.00	Profit and Loss—	
		·805 × 10	
		Sinking Fund instalment	8.05
		Interest on Sinking Fund	1.95
			10.00
		Cash on redemption	100
	£110.00		£110.00

It sometimes happens that a sinking fund requires "mending" or correction after having been in force for a time. The change may become necessary from various causes, a deficiency or a surplus in the income from the investments, consolidation, and other circumstances, and by way of conclusion we shall assume a case containing the principal features of one of these elements, show one of the modes of rectification that may be applied, and explain as we proceed. Our starting point is a 5 per cent. loan of £10,000 to be repaid at the end of 10 years. It is decided to create an invested sinking fund, and it is further assumed that the investments which the fund will represent, will yield a rate of 3 per cent. per annum. Now the amount of £1 per annum at .03 upon 1 for 10 years

$$= 11.46388 \frac{(1.03)^{10} - 1}{.03}, \text{ and } \frac{1}{11.46388} = .0872305$$

the sinking fund instalment for £1. For £10,000, it is (.0872305 × 10,000) = £872.305; and the table may be prepared as under, incidentally

$$\text{observing that } \frac{10,000}{872.305} = 11.4638, \text{ which is the}$$

amount of £1 per annum at 3 per cent. for 10 years.

We may, therefore, prepare our table on this basis—

Year	Amount of Fund at beginning of each year.	Interest yielded by Investments.	Annual Sinking Fund.	Amount of Fund at end of each year.
	£	£	£	£
1	—	—	872.305	872.305
2	872.305	26.16915	872.305	1770.77915
3	1770.77915	53.12337	872.305	2696.20752
4	2696.20752	80.88622	872.305	3649.39874
5	3649.39874	109.48196	872.305	4631.18570
6	4631.18570	138.93557	872.305	5642.42627
7	5642.42627	169.27278	872.305	6684.00405
8	6684.00405	200.52012	872.305	7756.82917
9	7756.82917	232.70487	872.305	8861.83904
10	8861.83904	265.85517	872.305	9999.99921

It will be seen that at the end of the fifth year the fund has reached a total of £4631.18570. Now let us suppose that it be found in the actual working of the fund that the accumulations only amount at the end of 5 years to £4,470, thus realising in that time a rate of a trifle under $1\frac{1}{4}$ per cent. There are various methods of ascertaining the rate; the following will be sufficient for our purpose—

$$\frac{4,470}{872.305} = 5.12435.$$

The amount of £1 per annum at 1 per cent. is 5.10100.

The amount of £1 per annum at $1\frac{1}{4}$ per cent. is 5.12657.

It will thus be seen that the true rate is between 1 and $1\frac{1}{4}$ per cent.

Now—

$$\begin{aligned} & .01 + \frac{5.10100 - 5.12435}{5.10100 - 5.12657} \times (.0125 - .01) \\ & = .01 + \frac{.02335}{.02557} \times .0025 \\ & = .01 + .91317 \times .0025 = .01 + .0022829 \\ & = .0122829 \text{ upon 1, or } 1.2282\% \text{ (say).} \end{aligned}$$

Applying the ascertained rate, which is sufficiently near for our requirements, we have—

INTEREST @ 1.2282%.

Instalment at end of 1st year . . .	£ 872.305
Interest	10.7136
Instalment at end of 2nd year . . .	872.305
	1755.3236
Interest	21.5588
Instalment at end of 3rd year . . .	872.305
	2649.1874
Interest	32.5373
Instalment at end of 4th year . . .	872.305
	3554.0297
Interest	43.6505
Instalment at end of 5th year . . .	872.305
	£4469.9852

As is shown in the concluding table of this sketch, the rate of 1.22829 per cent. leaves a difference at the end of the fifth year of only .0067, a difference which may be neglected.

The present position of the fund is that it contains £4,470. Now let us suppose that it is estimated that the future sinking fund instalment will yield a 2 per cent. rate, as will also the amount of the existing investment. On this basis we may

proceed to adjust the sinking fund instalment for the unexpired term of the loan.

The present investments amount to . . .	£ 4470
which it is estimated will yield 2% p.a. (i.e. £89.40); and	
£89.40 accumulated for 5 years at 2% will amount to	465.24117
The original Sinking Fund instalment of £872.305 accumulated for 5 years at 2% will amount to	4539.51011
Total	9474.75128
Leaving amount to provide	525.24872
	£10,000

The necessary annual sinking fund instalment to arrive at £525.24872 in 5 years at 2 per cent. is—

$$\frac{(1.02)^5 - 1}{.02} = 5.20404, \text{ and } \left(\frac{1}{5.20404} \right) = .192158$$

$$\therefore .192158 \times 525.24872 = £100.930745 \text{ the instalment.}$$

The adjusted instalment is, therefore—

$$\begin{aligned} & 872.305 \\ & 100.930745 \\ \hline & £973.235745 \end{aligned}$$

There are other modes, and many other varying circumstances, which might be employed and described, but the foregoing must suffice for the purpose of this brief sketch.

That this new rate of £973.235745 will attain the desired object, we may indicate by the following tabulation, viz.—

Present amount of investments . . .	£ 4470
Interest @ 2%	89.4
Instalment @ end of 6th year . . .	973.23574
	5532.63574
Interest @ 2%	110.65271
Instalment @ end of 7th year . . .	973.23574
	6616.52419
Interest @ 2%	132.33048
Instalment @ end of 8th year . . .	973.23574
	7722.09041
Interest @ 2%	154.44180
Instalment @ end of 9th year . . .	973.23574
	8849.76795
Interest @ 2%	176.99535
Instalment @ end of 10th year . . .	973.23574
	£9999.99904

The full actual experience of the transaction, assuming the realisation of the estimate for the

unexpired term of the fund may now be exhibited as under—

Year.	Amount of Fund at beginning of each year.	Interest received on Investments.	Annual Sinking Fund.	Amount of Fund at end of each year.
	£	£	£	£
1	—	—	872-305	872-305
2	872-305	10-7144	872-305	1755-3244
3	1755-3244	21-5604	872-305	2649-1898
4	2649-1898	32-5397	872-305	3554-0345
5	3554-0345	43-6538	872-305	4470
6	4470	89-4000	973-23574	5532-63574
7	5532-63574	110-65271	973-23574	6616-52419
8	6616-52419	132-33048	973-23574	7722-09041
9	7722-09041	151-44180	973-23574	8849-76795
10	8849-76795	176-99535	973-23574	9999-99904

SLIP SYSTEM OF POSTING.

The advent of the typewriter and of the adding machine has paved the way to the introduction of numerous time and labour-saving devices, enabling business records to be more speedily and accurately dealt with.

SALES.—This is particularly so with regard to the sales records, and an outline of a slip system of dealing with this department must be of interest and profit.

When ledger accounts are entered up from original slips, dockets or documents, instead of from a subsidiary book into which such slips, dockets, or documents have first been copied, the system is spoken of as the *slip system*. Such a system has long been in use in banks, where the postings to the customers' ledgers are made direct from the paying-in slips, cheques, bills, etc.

In business houses, the methods of posting from the original invoices vary according to the system employed, and to the nature of the subdivision of the sales ledgers—whether alphabetical, geographical, or departmental.

Generally speaking, every business provides for the sectional balancing of its books, with, in consequence, an adjustment or control account in the General Ledger for each ledger in use.

In the "slip system," invoices are typed in multiple copies—one for the customer and the others for the sales records. The number of copies typed would depend upon the nature of the records kept in the particular business. Where no Sales Day Book is kept, the total of the sales may be obtained by means of an adding machine attached to the typewriter, or by means of a separate adding machine through which the amount of each invoice is brought on to a slip and the daily, weekly, or monthly total sales obtained.

This total would be dealt with through the General Ledger by being debited to "Debts Collection Account" and credited to "Sales Account."

The postings to the debit of customers would be effected direct from the carbon copy invoices, and the copy invoices would, after being posted to the ledger, be filed in numerical order.

Where there are subdivisions of the Sales Ledger these copy invoices would, prior to posting, be sorted into batches corresponding to the ledgers into which they have to be posted. In such cases, the total of each batch would be separately ascertained and treated in the General Ledger in separate adjustment or control accounts.

Thus, the total of the invoices to be posted to the debit of customers in the "A to K" ledger would, in the General Ledger, be debited to the "A to K Debts Collection Account," and the total of those to be posted to the debit of customers in the "L to P" Ledger, debited to the "L to P Debts Collection Account."

Each invoice and its copy or copies would be printed with numbers to correspond and fastened in sets, each set being detached only when typed and ready for issue. When being sorted for filing after having been posted to the ledger, they would be brought into numerical order, and any set spoiled would be placed in the file complete and according to its number so that numbers will run consecutively and none be missing.

If desired, invoices relating to different departments could be printed upon different coloured paper to simplify their sorting for the purpose of obtaining the departmental sales totals.

Credit notes issued to customers would be treated on similar lines, but as they have to be posted to the credit of customers, their total would be credited in the General Ledger to the Debts Collection Account and debited to Sales Account.

Should it be desired to have a Day Book showing the total of the sales, the method is to use loose sheets, numbered consecutively upon which a carbon copy of each invoice is taken, the sheet moving through the typewriter until filled. The total of the sheet is then typed, carried forward, and so on, until it is desired to break the cast for posting to the General Ledger.

The sheets are filed in numerical order, and then constitute a typewritten Day Book, giving the *facsimile* of every invoice issued. The postings to the customers' accounts may be done from the invoices or from the sheets.

Further, the invoice "sets" may be so fixed together as to include an envelope for the dispatch of the invoice, such envelope being addressed, in carbon, when the customer's name and address are typed upon the invoice on the top of the set.

CASH.—Remittances received in settlement of debtors' accounts should be first arranged in batches according to the ledgers to which they have to be posted.

They would then be entered upon sheets, a separate sheet being used for each ledger, and

posted from the sheets to the credit of the customers. The totals of the sheets would be entered in the Cash Book and posted from the Cash Book to the credit of the different Debts Collection or Control Accounts in the General Ledger. The sheets should be ruled with the usual discount and cash columns, and when filed, form a loose-leaf Cash Book.

They are filed in numerical order and their numbers noted in the Cash Book against the totals carried there.

All remittances should be paid into the bank in full—any cash required for office use being obtained by a cheque drawn on the bank.

PURCHASES.—A monthly pay-day would be fixed and all invoices received during the month would be grouped in alphabetical order, each creditor's invoices being brought together. The total due to each creditor for the month would be summarised on a slip and the amounts brought on to suitably analysed sheets for the purpose of classifying the purchases to departments. These sheets form the tabular Purchase Journal, and being provided with extra money columns for cash and discount form at the same time a personal ledger. The cheques issued are posted to the cash column against the item being paid, and a creditors' ledger is thus not necessary.

At stocktaking, a list is made of all invoices received since the previous pay-day and all accounts not paid, and this list forms the item of Sundry Creditors in the Balance Sheet.

When the creditors return a receipt for a remittance, the receipt would be attached to the bundle of invoices it covers and the whole suitably filed.

SOLA.

Foreign bills are frequently drawn in a set (see **FOREIGN BILL**), that is, drawn in three parts. Sometimes, however, one bill or one part only is used, and the instrument is then known as a "sola" bill of exchange, and is expressed to be so in the body of it, thus: "Twenty days after date pay this sola bill of exchange," etc.

SOLE TRADER.

A person who carries on business entirely on his own account, in contradistinction to a group of persons trading in partnership or as a joint stock company.

SOLICITORS' COSTS, AUDITORS AND.

(See **AUDITING**, p. 115.)

SOUNDING IN DAMAGES.

An action is technically said to sound in damages when it is brought, not for the specific recovery of lands or goods, or for the granting of an injunction, but for the recovery of damages only, as in actions of covenant, trespass, etc.

SPECIAL AGENT.

(See **AGENT**.)

SPECIAL DEFENCE.

In the ordinary course any defence to an action at law can be raised by the defendant in his own behalf; but if the defence is one which, when raised, does not affect the validity of a contract but simply gives the defendant an opportunity of raising a point which is legally open to him, this is a special defence, and, speaking generally, the law demands that a defendant who wishes to raise such a point must plead it specially in the High Court or give notice of it in an action in the County Court. The following are illustrations: Infancy, Statutes of Limitations, Gaming, Statute of Frauds, Sale of Goods Act, Public Authorities Protection Act. The existence of any liabilities under contracts made in connection with the first five of these is only abated by special statutes, and the liability in the case of any tort under the sixth is only excused by the Statute of 1893. There is nothing otherwise affecting either the validity of the contract in the first case or the liability for the tort in the latter. In order, however, that these weapons of defence shall be made use of, the law demands that the points shall be raised as a special defence in an action, and that none of them shall be of any avail without such defence being put forward.

SPECIAL DUTIES OF AUDITORS.

(See **AUDITING**, p. 68.)

SPECIAL MANAGER'S ACCOUNTS.

(See **BANKRUPTCY ACCOUNTS**, p. 182; **LIQUIDATORS, ACCOUNTS OF**, p. 689.)

SPECIAL RESOLUTION.

(See **RESOLUTIONS, LIMITED COMPANY**.)

SPECIALTY CONTRACT.

A contract under seal, so named, in contradistinction to a simple contract, because of the special circumstances attendant upon the method of its execution. (See **DEED**.)

SPECIALTY DEBTS.

These are debts which are created by deed, and as such take a higher standing than debts by simple contract. At one time they enjoyed a priority over simple contract debts, but the preference was taken away by *Hinde Palmer's Act* (*q.v.*).

SPECIFIC LEGACY.

(See **LEGACIES**.)

SPECIFIC PERFORMANCE.

Every person who enters into a contract is bound to perform his obligation under the contract or to compensate the other party by means of damages.

Damages are the compensation awarded for a breach of a contract. In certain cases, however, it is clear that damages cannot form an adequate recompense for breach of contract. Suppose a purchaser has a special reason for becoming the owner of a certain estate which he has contracted to buy. It is probable that no pecuniary sum will satisfy him for the loss of the estate, and then his loss cannot be estimated in money. Provided that there is no other obstacle in the way, the Court will not be content with awarding damages. It will decree that the vendor shall carry out his part of the contract and convey the estate to the purchaser. This is a decree of specific performance, that is, the actual performance of what the vendor has undertaken to do.

This remedy is almost exclusively confined to the Chancery Division of the High Court of Justice, but now and then one hears of it in the King's Bench Division, especially in cases arising out of the Sale of Goods Act, 1893, for it is specially provided by that Statute that the relief of specific performance may be extended to the case of the sale of articles of peculiar value, especially when it is impossible for the buyer to obtain others of the same kind in the open market. Specific performance is the opposite of injunction. A refusal to obey an order for specific performance

renders the offender liable to attachment for contempt of court.

SPLITTING THE DIVIDEND OR INTEREST.

Two important factors to be considered in arriving at the yield of an investment are (1) whether the purchase is made at a premium or a discount; and (2) whether the security is definitely redeemable on a given date, or whether it may be regarded as being irredeemable. If the investment be a terminable one, the difference between the prices of purchase and redemption should be extinguished during the currency of the transaction. This may be effected by calculating the true yield on the basis of compound interest, and what is sometimes termed splitting the dividend or interest by giving to capital and to income their due proportions. Let us take, for example, a 5 per cent. bond for £100 purchased on the 1st January, 1918, for £90, the interest being payable half-yearly on the 30th June and 31st December, and the bond being definitely redeemable in five years on the 31st December, 1922. Here a little actuarial calculation affords us the true yield of 3·716 per cent. half-yearly which is sufficiently near for our purpose.

We may, therefore, now construct the following table—

Date. (1)	Capital outlay and interest at true rate of yield therein and on excess of true yield over nominal yield. (2)	Interest at 3·716% upon amounts in column (2) (3)	Interest receivable half-yearly. (4)	Excess of amounts in column (3) over those in column (4) to be debited to Bond A/c and credited to Interest A/c. (5)	Total of columns. (4) and (5) (6)
1918. Jan. 1	£ 90·	£	£	£	£
June 30	·84440	3·34440	2·50	·84440	3·34440
Dec. 31	90·84440 ·87577	3·37577	2·50	·87577	3·37577
1919. June 30	91·72017 ·90832	3·40832	2·50	·90832	3·40832
Dec. 31	92·62849 ·94207	3·44207	2·50	·94207	3·44207
1920. June 30	93·57056 ·97708	3·47708	2·50	·97708	3·47708
Dec. 31	94·54764 1·01339	3·51339	2·50	1·01339	3·51339
1921. June 30	95·56103 1·05104	3·55104	2·50	1·05104	3·55104
Dec. 31	96·61207 1·09010	3·59010	2·50	1·09010	3·59010
1922. June 30	97·70217 1·13061	3·63061	2·50	1·13061	3·63061
Dec. 31	98·83278 1·17262	3·67262	2·50	1·17262	3·67262
	100·				

The table is almost self-explanatory, interest being calculated at the ascertained true rate of interest on the purchased price. On 30th June, 1918, interest is computed on £90 which equals 3'34440, and the excess of that sum over the interest receivable as per column 4 is '84440, which is added to the purchase price, interest for the second half of the year being calculated on £90'84440 as shown. Subsequent accretions are similarly computed and treated.

We need only show the first and second year's figures of the bond and interest accounts, viz.—

BOND ACCOUNT			
1918.		£	
Jan. 1.	To Cash	90'	
June 30.	" Interest		'84440
Dec. 31.	" "		'87577
1919.			
June 30.	" "		'90832
Dec. 31.	" "		'94207

INTEREST ACCOUNT			
1918.		£	
June 30.	To P. & L. A/c	3'34440	
Dec. 31.	" "		3'37577
			<u>£6'72017</u>
1919.		£	
June 30.	To P. & L. A/c	3'40832	
Dec. 31.	" "		3'44207
			<u>£6'85039</u>

1918.		£	
June 30.	By Cash & Tax	2'50	
	" Bond A/c		84440
Dec. 31.	" Cash & Tax	2'50	
	" Bond A/c		'87577
			<u>£6'72017</u>
1919.		£	
June 30.	By Cash & Tax	2'50	
	" Bond A/c		'90832
Dec. 31.	" Cash & Tax	2'50	
	" Bond A/c		'94207
			<u>£6'85039</u>

It will be seen that interest account is credited with the half-yearly interest received, that it is also credited with the sums shown in column 5 of the schedule, and that it is debited with the sums appearing in column 3 of that statement.

The amount received on redemption should close the bond account. Accrued interest is, of course, interest which has accrued to the date of purchase, and is, therefore, a credit to the purchase price.

SPOILED STAMPS.

It happens not infrequently that documents are prepared, for which stamps are required, and that these documents are not utilised or acted upon. In order to reclaim the amount paid for the stamps, whether adhesive or impressed, application must be made to the Spoiled Stamp Office, Somerset House, and if a satisfactory explanation is forthcoming the amount paid in respect of the stamps, less a certain discount, will be refunded, or stamps of an equal amount will be granted in lieu of the spoiled stamps. Application must be made, however, within two years of the date of the spoiling of the stamps or the execution of the document, otherwise the claim will not be considered. If it is a banker carrying on business at a distance greater than ten miles from London

who makes a claim in respect of spoiled stamps, he must do so through a London agent.

Whenever any claim is made in respect of spoiled stamps, the applicant is required to fill up a form, which is supplied by the authorities at Somerset House.

SPREADING EXPENDITURE.

(See AUDITING, p. 83; BALANCE SHEET, p. 155.)

STABLE EXPENSES.

(See HORSEKEEP and STABLE EXPENSES.)

STAMP AFFIXING MACHINES.

(See OFFICE MACHINES AND APPLIANCES.)

STAMP DUTIES.

These are duties which are imposed upon the parchment or paper on which certain legal documents are written. Under certain statutes, but chiefly under the Stamp Act, 1891, the amounts of the various duties are fixed, and the payment of the stamp duty is a condition precedent to allowing the documents to be produced as evidence in a court of law. In some cases, however, documents may be stamped after the proper time has elapsed upon payment of certain penalties, but this post-stamping is never permitted when the documents are any of the following—

- Bills of Exchange.
- Contract Notes.
- Letters of Allotment.
- Letters of Renunciation.
- Proxies.
- Receipts.
- Scrip Certificates.
- Share Warrants.
- Voting Papers.

An agreement, or memorandum of agreement, under hand must be stamped within fourteen days, and a deed within thirty days, of the date of the execution of the instrument.

In most cases an impressed stamp is required, but an adhesive stamp may be used in the following—

- Agreements liable to a duty of 6d.
- Bills of exchange payable on demand. This includes cheques.
- Certified copies of or extracts from registers of births, etc.
- Charter-parties.
- Contract notes where the amount is less than £100.
- Leases of dwelling houses, or parts thereof, furnished or unfurnished, for any definite period not exceeding a year, where the rent is not more than £25 for a furnished, and £10 for an unfurnished, house.
- Letters of renunciation.
- Notarial acts.
- Policies of fire insurance.

Protests of bills of exchange.
Proxies, where the duty is 1d.
Receipts.
Voting papers.
Warrants for goods.

The following is a list of the principal stamp duties—

	£	s.	d.
Admission—			
To the degree of a barrister	50	0	0
As solicitor or proctor, or writer to the signet	25	0	0
As student at any Inn of Court, or student of King's Inn, Dublin	25	0	0
As Fellow of College of Physicians	25	0	0
As burgess, by birth, apprenticeship, or marriage, England or Ireland	1	0	0
As burgess, on any other ground	3	0	0
Faculty as a Notary Public, England	30	0	0
Faculty as a Notary Public, Scotland or Ireland	20	0	0
As a burgess in Scotland	5	0	
Affidavit , or statutory declaration	2	6	
Agreement , or memorandum of agreement, under hand, not otherwise charged		6	
Agreement for lease of a furnished house for less than a year, the rent not exceeding £25	5	0	
(Agreement for lease, other than the above, same as lease.)			
Appointment of new trustee	10	0	
Appraisement or valuation of any estate of effects where the amount of the appraisement does not exceed £5		3	
Not exceeding £10		6	
" £20		1	0
" £30		1	6
" £40		2	0
" £50		2	6
" £100		5	0
" £200		10	0
" £500		15	0
Exceeding £500	1	0	0
Apprenticeship indentures		2	6
Arms , Grant of	10	0	0
Articles of Clerkship to solicitor—			
In England or Ireland	80	0	0
In Scotland	60	0	0
Award		10	0
Bill of Exchange (inland bill)—			
When payable on demand (or within three days after date or sight), for any amount, or when the amount does not exceed £10		2	
Exceeding £10 and not exceeding £25		3	
" £25 " " £50		6	
" £50 " " £75		9	
" £75 " " £100	1	0	

Bill of Exchange (inland bill)—(contd.) £ s. d.

When the amount exceeds £100, 1s. for the first £100, and 1s. for each additional £100 or fraction thereof.

Foreign bills of exchange drawn out of the United Kingdom, but payable in the United Kingdom, are stamped in the same manner as inland bills. Foreign bills of exchange drawn and expressed to be payable out of the United Kingdom, but indorsed, negotiated, or actually paid within the United Kingdom, are stamped as inland bills when they do not exceed £50.

Exceeding £50 and not exceeding £100 6

Exceeding £100, for every £100 or any part thereof 6

(Promissory notes are stamped in the same manner as bills of exchange, except that all promissory notes are subject to an *ad valorem* duty.)

Bill of Lading 6

Bill of Sale, Absolute. (See CONVEYANCE.)

Bill of Sale, Conditional. (See MORTGAGE.)

Bonds.—For securing an annuity, where the payments are for the term of life, or other indefinite period, for every £5, and every fractional part of £5 payable—

(a) If as primary security 2 6

(b) If as collateral security 6

For securing an annuity where the total amount is ascertainable, or for the payment of money, same as mortgage.

For customs or excise duties, same as mortgage bond, but not to exceed 5s.

For other duties not specifically charged (including fidelity bonds), same as mortgage bond, but not to exceed 10s.

On obtaining letters of administration (where the amount exceeds £100) 5 0

Capital Duty (Share)—

Companies and corporations with limited liability, on every £100 of nominal capital 1 0 0

Capital Duty (Loan)—

Issues by local authorities, companies and corporations, on every £100 secured 2 6

But 2s. in the £ is repayable if the capital is applied in the conversion of an existing loan.

Cards (playing), for every dozen packs . 3 9

Certificate of solicitor, law agent, writer to the signet, notary public, conveyancer, special pleader, and draughtsman in equity (yearly).

Certificate of solicitor, etc.—(contd.)

If practising within ten miles of the General Post Office, London, or in the city or shire of Edinburgh, or in the city of Dublin or within three miles thereof	9	0	0
If practising elsewhere	6	0	0
(N.B.—During the first three years after admission one half only of these fees are payable).			
Certificate of birth, baptism marriage, death, or burial	1		
Charter-Party	6		
Cheque	2		
Collateral Security, for each £100	6		
Contract Note—			
Not exceeding £100	6		
Exceeding £100, but not exceeding £500	1	0	0
" £500 " " £1,000	2	0	
" £1,000 " " £1,500	3	0	
" £1,500 " " £2,500	4	0	
" £2,500 " " £5,000	6	0	
" £5,000 " " £7,500	8	0	
" £7,500 " " £10,000	10	0	
" £10,000 " " £12,500	12	0	
" £12,500 " " £15,000	14	0	
" £15,000 " " £17,500	16	0	
" £17,500 " " £20,000	18	0	
" £20,000 " " "	1	0	0

Continuation notes are charged on one only of the two transactions embraced. Option contract notes are charged with half the above rates only, unless the option is a double one. Contract notes following duly stamped option contracts are relieved from half the duty.

Contract or grant for payment of a superannuation annuity; for every £5 or fractional part of £5

Conveyance or transfer—

Bank of England stock 15 6

Colonial debenture stock or funded debt, for every £100 or fractional part of £100, of nominal value transferred 5 0

Property other than such stock—

Where the purchase money does not exceed £5 1 9

Exceeding £5, and not exceeding £10 2 6

 " £10 " " £15 3 9

 " £15 " " £20 4 0

 " £20 " " £25 5 0

For every additional £25 up to £300 5 0

For every £50, if exceeding £300 10 0

Not otherwise charged 10 0

N.B.—In cases where the consideration does not exceed £500 and the instrument contains a certificate as required by the Finance (1909-10)

Conveyance of transfer—(contd.)

Act, 1910, section 73, that the transaction does not form part of a larger transaction or of a series of transactions in respect of which the consideration exceeds £500, duty is charged at half the above rates.

Conveyances by way of gift *inter vivos* are charged as conveyances on sale. Exceptions are made for marriage settlements, and certain gifts of property for preservation of open spaces, and for conveyances to appoint new trustees, etc.

Copy or Extract (attested or authenticated), the same duty as the original, but not to exceed 1 0

Copyhold and Customary Estates—

If on sale, mortgage, or demise, the *ad valorem* duties under Conveyance, Mortgage, or Lease. Upon any other occasion—Surrender or grant made out of Court, or the memorandum thereof, and copy of court-roll of any surrender or grant made in Court 10 0

Corporate and Unincorporate Bodies—

Upon the *net* annual value, income or profits accrued in respect of all real or personal property vested in such bodies per cent. 5 0 0

(Subject to certain exceptions laid down in the Customs and Inland Revenue Act, 1885.)

Covenant—

For repayment of money. (See MORTGAGE.)

For original creation and sale of any annuity. (See CONVEYANCE.)

For an annuity (except on original creation and sale) or other periodical payments. (See BOND.)

Separate Deed of, made on occasion of sale or mortgage, but not being an instrument chargeable with *ad valorem* duty as a Conveyance or Mortgage: same duty as a Conveyance on Sale, or a Mortgage, but not to exceed 10 0

Declaration. (See AFFIDAVIT.)

Declaration of Trust, not being a will or settlement 10 0

Deed of any kind not charged under some special head 10 0

Demise. (See LEASE.)

Deputation or appointment of a game-keeper

Duplicate or Counterpart—

Same duty as original, but not to exceed 5 0

Ecclesiastical Licences—

To hold the office of lecturer, etc. . .	£	s.	d.
For licensing a building for divine service, etc., and any chapel for solemnising marriages . . .	10	0	0

Licence not otherwise charged . . .	2	0	0
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Equitable Mortgages under hand only—

For every £100 or part thereof . . .	1	0	
--------------------------------------	---	---	--

Hire Purchase Agreements—

Under hand	6		
Under seal	10	0	

Insurance Policies (Life)—

For any sum not exceeding £10 . . .	1		
-------------------------------------	---	--	--

Exceeding £10, and not exceeding £25	3		
--------------------------------------	---	--	--

Exceeding £25, and not exceeding £500, for every £50 or fractional part thereof	6		
---	---	--	--

Exceeding £500, and not exceeding £1,000, for every £100, or fractional part thereof	1	0	
--	---	---	--

Exceeding £1,000, for every £1,000, or any fractional part thereof . . .	10	0	
--	----	---	--

Accidental death, or personal injury, or periodical payments during sickness Loss or damage to property . . .	6		
---	---	--	--

Indemnity against loss under the Employers' Liability Act, or the Workmen's Compensation Act—	6		
---	---	--	--

Where the annual premium does not exceed £2	6		
---	---	--	--

Where the annual premium exceeds £2 :			
---	--	--	--

If by agreement under hand . . .	6		
----------------------------------	---	--	--

If by deed	10	0	
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Marine—

(1) Where premium or consideration does not exceed the rate of 2s. 6d. per cent.	1		
--	---	--	--

(2) Otherwise—**(a) Voyage.**

Where the sum insured—			
------------------------	--	--	--

Does not exceed £250	3		
--------------------------------	---	--	--

Exceeds £250 but not £500	6		
-------------------------------------	---	--	--

" £500 " £750	9		
-------------------------	---	--	--

" £750 " £1,000	1	0	
---------------------------	---	---	--

" £1,000, for every £500 and/or fraction	6		
--	---	--	--

(b) Time.			
-----------	--	--	--

(i) Where insurance is for a period not exceeding six months . . .	Three times amount payable on a voyage.		
--	---	--	--

(ii) Where insurance is for a period more than six months but less than twelve months		
---	--	--

(ii) Where insurance is for a period more than six months but less than twelve months	Six times amount payable on a voyage.		
---	---------------------------------------	--	--

(3) For a continuation clause, extra . . .	6		
--	---	--	--

(4) (a) Where the premium or consideration does not exceed 2s. 6d. per cent., but is subject to a contingent increase, to be treated as (1).			
--	--	--	--

Insurance Policies (Marine)—(contd.)

(b) If through the contingency the premium or consideration is increased so as to exceed 2s. 6d. per cent.

Such additional sum as required to represent the additional duty payable.

Leases—

A dwelling house, or a part thereof, for a definite period not exceeding one year, the rent not exceeding £10 per annum

A furnished dwelling house, or apartments in the same, for a definite period less than a year, the rent for the term not exceeding £25 per annum

Lands or tenements at the following rents, and for the periods stated—

Exceeding.	Not Exceeding.	Up to 35 years.	35 years to 100 years.	Over 100 years.
	£5	£ s. d. 1 0	£ s. d. 6 0	£ s. d. 12 0
	£10	2 0	12 0	1 4 0
	£15	3 0	18 0	1 16 0
	£20	4 0	1 4 0	2 8 0
	£25	5 0	1 10 0	3 0 0
	£30	10 0	3 0 0	6 0 0
	£35	15 0	4 10 0	9 0 0
	£40	1 0 0	6 0 0	12 0 0
	£100 (for each £50, or fractional part of £50)	10 0	3 0 0	6 0 0

An agreement for a lease not exceeding 35 years is stamped the same as an actual lease.

Letters of Allotment and Renunciation—

Less than £5	1		
£5 and upwards	6		

Letters Patent (Grant of honours or dignities)—

Duke . . . . .	.350	0	0
Marquis . . . . .	.300	0	0
Earl . . . . .	.250	0	0
Viscount . . . . .	.200	0	0
Baron . . . . .	.150	0	0
Baronet . . . . .	.100	0	0
Precedence . . . . .	.100	0	0

Congé d'élire to elect—

Archbishop or bishop . . . . .	.30	0	0
Any other honour . . . . .	.30	0	0
Change of name or arms (if done in accordance with the terms of a will) . . .	.50	0	0

Letters Patent (Grants of honours)—(contd.)			£	s.	d.				£	s.	d.
Change of name or arms upon a voluntary application			10	0	0	Any other kind of power of attorney			10	0	
Letters Patent, for inventions—						Procurator, Deed or other instrument of			10	0	
Application for provisional protection			1	0	0	Promissory Note. (See BILL OF EXCHANGE.)					
Filing complete specification			3	0	0	Protest of Bill of Exchange—					
On the notice of a desire to have the patent sealed			1	0	0	The same duty as the bill itself, but not to exceed			1	0	
The duration of a patent may extend up to fourteen years, but this duration depends upon the payment of certain fees each year, otherwise the patent lapses at the end of the fourth year. The payment in respect of each year must be made before the commencement of the year as follows—						Receipts for £2 and upwards			2		
For the 5th year			5	0	0	Renunciation, Letter of. (See LETTER OF RENUNCIATION.)					
" 6th "			6	0	0	Revocation of any trust of property, not being a will			10	0	
" 7th "			7	0	0	Scrip Certificate			2		
" 8th "			8	0	0	Securities (transferable by delivery)—					
" 9th "			9	0	0	(1) Colonial Government Securities, and other securities dated between 3rd June, 1862, and 7th August, 1885, of which the interest is payable in the United Kingdom, same as mortgage.					
" 10th "			10	0	0	(2) Other securities, for every £10 or fractional part of £10			1	0	
" 11th "			11	0	0	(3) Foreign share certificates, for every £25 or fractional part of £25 . .			3		
" 12th "			12	0	0	Settlements—					
" 13th "			13	0	0	Any deed whereby a definite sum or share is settled upon or for the benefit of a person, for every £100 or fractional part of £100			5	0	
" 14th "			14	0	0	Share Warrant, or stock certificate to bearer—					
These fees are subject to revision, and are exclusive of certain other small charges.						(1) <i>British.</i> The duty is three times the transfer duty.					
Marketable Securities. (See separate article.)						(2) <i>Colonial.</i> For every £100 and fraction of £100 of the nominal value of stock			5	0	
Marriage Licence—						(3) <i>Foreign.</i> For every £10 and also for any fractional part of £10 of the nominal value of the share or stock . .			4	0	
Special			5	0	0	Voting Paper or Proxy			1		
Other			10	0		Where a proxy is a general one, that is, where it gives the right to vote at more than one meeting, or the adjournment thereof, or at meetings generally, the duty is 10s.					
Moneylenders' Registration			1	0	0	Warrant for Goods			3		
Mortgages—						Many other duties are paid by means of stamps, such as Estate Duty, Legacy Duty, Succession Duty, Mineral Rights Duty, etc.					
Not exceeding £10			3			Penalties. The following are the penalties usually enforced in cases of failure to stamp documents at the proper time—			£	s.	d.
" £25			8			Agreements under hand, after the expiration of fourteen days			10	0	0
" £50			1	3		Charter-parties, within seven days from their first execution			4	6	
" £100			2	6		Charter-parties, after seven days but within a month			10	0	0
" £150			3	9							
" £200			5	0							
" £250			6	3							
" £300			7	6							
Exceeding £300, for every £100 and fractional part thereof			2	6							
Transfer of Mortgage, per £100 . . .			6								
Reconveyance, release, per £100 . .			6								
Notarial Act (of any kind) except protests			1	0							
Passport			6								
Patents. (See LETTERS PATENT.)											
Power of Attorney—											
To receive prize-money or wages . .			1	0							
For sale, transfer, or acceptance of any of the Government funds not exceeding £100, nominal amount . .			2	6							
In any other case			10	0							
For receipts of dividends or interest of any stock, for one payment . . .			1	0							
In any other case			5	0							
To vote at a meeting			1								

Penalties—(contd.)

	£	s.	d.
Receipts within fourteen days after they have been given	5	0	0

Receipts, after fourteen days but within a month	10	0	0
--	----	---	---

(N.B.—After a month receipts cannot be stamped under any circumstances.)

Other instruments (except those which cannot be stamped after execution)	10	0	0
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STAMPS, ADHESIVE.

(See ADHESIVE STAMPS.)

STATE INSURANCE.

(See HEALTH AND UNEMPLOYMENT INSURANCE DEDUCTIONS.)

STATEMENT IN LIEU OF PROSPECTUS.

Where a public company does not issue any prospectus on its formation, it is necessary to file a statement as required by Section 82 of the Companies (Consolidation) Act, 1908, before any allotment of shares or debentures can take place. This statement in lieu of prospectus is to be signed by every person named therein as a director or proposed director of the company. The form of the statement is contained in the second schedule to the Act, and generally the particulars required are such as are required to be included in a prospectus under Section 81. In the case of the statement, however, it is unnecessary to give particulars of the memorandum as this document is already on the Registrar's file. Particulars as to the holders of founders' shares and voting powers are not required. (See also PROSPECTUSES, SHARES, CLASSES OF.)

STATEMENT OF ACCOUNT.

A copy of a customer's account forwarded to him periodically, usually monthly, and made up to the date customary for payment by a certain date for full discount terms.

The Statement gives the dates on which goods have been supplied since the last Statement was rendered, and the amounts of the invoices for same. Should previous accounts rendered not be paid, the totals of each are also shown, together with a note of the discount which will be allowed for prompt payment against each of such amounts of accounts rendered.

STATEMENT OF AFFAIRS.

(See BANKRUPTCY ACCOUNTS, p. 157; LIQUIDATORS, ACCOUNTS OF, p. 648 and 665.)

STATIONERY.

(See PRINTING AND STATIONERY.)

STATISTICS.

Statistics are defined by Professor Bowley as "numerical statements of facts in any department

of inquiry, placed in relation to each other; statistical methods are devices for abbreviating and classifying the statements and making clear the relations." From the point of view of the accountant, the numerical facts which are placed in relation to each other are values in relation to production or output, or money in relation to commodities.

The books of a business are often classified under two heads, namely, financial and statistical; but, in reality, no sharp dividing line can be drawn, the accountants' statistics being supplied from the financial books as from the statistical. The division is merely a conventional one, conveying to the business man the fact that the system of costs used in his business are in part independent of the financial books, or perhaps, more truly stated, the costing system is not necessarily part of the ordinary routine of account-keeping in the business.

The accountant as a statistician must be prepared to extract from the books such facts as will in his judgment, when related to each other, throw light on the progress of the business, indicate what departments or shops are running economically, what leakages are taking place, and what economies may be effected without impairing efficiency. The manufacturer will keep statistical records of wages, administration expenses, costs of materials, sales, maintenance charges, and repairs. He will compare these values with output and with each other not only for each financial period, but for shorter intervals of time, in order that defects may be remedied immediately. The statistician keeps in mind long period changes and at the same time has his eye on short-term fluctuations. It is important for him to realise, from the facts related, when anything abnormal takes place in the relationship between the various costs and output from week to week, or month to month; but it is equally important that he watch the trend of these matters over longer periods. Examine, for example, the results of working a public undertaking as shown on page 880.

The compiling of such records as shown on next page is important as indicating the gradually increasing cost of working in relation to revenue from 1910 to 1914. It is immaterial in 1920 that the revenue in 1910 was £35,031 and expenses £23,687, but it is very material that cost in relation to revenue has risen 19 per cent. in five years. The reason must be sought and the cause removed. This evidently took place, and the percentage as well as the actual figures declined. The last year again shows a material advance, but this is explained by relation to facts—increased costs of labour and materials.

Such a table as that shown is generally recognised as a statistical analysis of financial results, but this is very incomplete, and without

Year.	1910.	1911.	1912.	1913.	1914.	1915.	1916.	1917.	1918.	1919.
1. Total Revenue	£35,031	£36,161	£37,182	£38,550	£41,190	£42,704	£45,141	£50,936	£63,082	£81,608
2. Working Exps.	£23,687	£25,569	£26,528	£31,514	£34,493	£30,956	£30,461	£31,993	£42,619	£64,718
3. % of Working Expenses on revenue	64.5	70.7	71.4	82.25	83.75	72.5	67	62.8	67.6	79.3
4. Gross Profit	£11,344	£10,592	£10,654	£7,036	£6,697	£11,748	£14,680	£18,943	£20,463	£16,890
5. Net Profit or Loss	£2,321	£1,492	£1,339	—	—	£2,417	£5,409	£8,611	£10,134	£5,666
	—	—	—	£2,327	£2,617	—	—	—	—	—

other data, conclusions cannot be correctly drawn. Output must be taken into consideration and the working expenses must be analysed. Statistics must be prepared relating output to costs (*e.g.* costs per ton of saleable coal raised; costs per unit of product sold; and coal costs per unit of product in electricity and gas undertakings; cost of cotton per lb., amount of waste per lb., cost per lb. when waste is eliminated, price of waste, wages per lb. of yarn produced or per thousand spindles in textile manufacture, are important statistics for short period examination).

In tramway working, costs per car-mile are of importance, and in railway goods traffic costs per ton-mile and revenue per ton-mile or train-mile are the basis of statistical investigation.

The labour and expense of statistical work is nothing compared with its advantages to a large business, and it is absolutely indispensable in these days of unrest and fluctuation in industry.

STATISTICAL REPORTS.—If statistics are compiled promptly and put quickly into use, they are of great value for purposes of comparison and measuring progress; but certain definite principles must be observed as to compilation, or the returns can be carried beyond the point of usefulness.

Three main principles should be kept in view, namely—

1. Returns should cover a period of some extent, but should not be so extensive as to have lost their value by reason of lapse of time.

2. The subject-matter of returns should be of considerable value, and not deal with particulars too meagre to have any bearing on the prosperity or failure of the business.

3. Statistics should be prepared in the simplest possible form, as the value of masses of figures cannot be grasped by the ordinary individual. In a word, they should deal with characteristics only, and should in themselves be a clear and condensed summary of the financial aspects of the business.

Dealing with principle 1, we are aware that no business flows steadily from day to day—weather may have an effect on the results of trading (*e.g.* a wet day's takings may be quite a different matter from those of a dry, bright day). Different departments may be affected by different sets of circumstances and, generally speaking, daily

returns of receipts, sales, orders, and the like would be of little value for comparison. Those on a given day in a given financial period would not be comparable with the same day in a succeeding financial period, hence daily returns in the average business would cover too short a period to be useful.

Such tendencies as have been referred to are compensated for over more or less long periods, and weekly returns would in most businesses be a satisfactory means of comparison. Even here, we must take into consideration the nearness of a given week to a holiday season, and where the holidays are movable, it may be that comparisons are not of great value (*e.g.* the week ending 29th May, 1920, would not compare favourably with the week ending 29th May, 1919, since in 1920, Whit week falls in the week ending 29th May, whereas it was a fortnight later in 1919). Obviously trade in these two weeks would vary, not only by reason of incidents peculiar to the given works or establishments, but by reason of the holiday season. Weekly returns, however, apart from these peculiarities, are more reliable for comparison. They allow time for daily fluctuations to average, and they disclose general tendencies. Thus a weekly cost sheet, as used in collieries, is a practical proposition, but a daily cost sheet would be futile. Again, the weekly cost sheet has the advantage of not delaying the information required. On the other hand, monthly reports present a truer average; but it may be that a month is too long to wait, as it must be remembered that comparisons are made for the purpose of making improvements and effecting economies where necessary, for eliminating waste, and generally reducing expenses, raising efficiency, and increasing profits.

In relation to principal 2, a railway company would not make a special return of the fact that, in 1920, there was an increase in the chartering of special trains of 50 per cent., as such fact would have little effect on the prosperity of the undertaking. Returns will be prepared only when they are likely to be such as will guide the policy to be adopted in respect of an important source of revenue. (See also *COST ACCOUNTS*.)

STATISTICAL DIAGRAMS AND GRAPHS.—The representation of statistics in diagrammatic

form is a popular method of recording the fluctuating financial facts of a business. It must, however, be remembered that diagrams are not intended to add to statistical investigation, but rather to indicate clearly and concisely the results obtained. They are not, from the accountant's point of view, mere pictures or illustrations: this aspect is of value only to the advertiser. Graphs and diagrams have no place in a business house, unless they can be put to some useful purpose in the business or show more clearly to the lay mind the truth and meaning underlying the tabulated data extracted from the books.

The chief use to which graphical representation may be put is to show the tendencies and changes in revenue, output, cost of materials, wages, oncost in successive financial periods or in successive weeks, months, or years, with a view to bringing into focus the lists of figures and interpreting them in terms of long and short period change, so indicating to the management the lines on which investigation into costs of production should proceed.

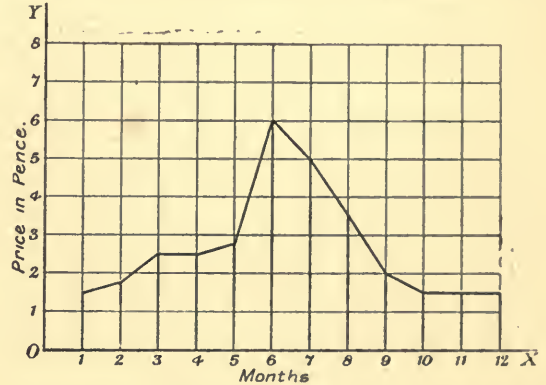
If we attempt to relate the price of cotton to various periods of time and to represent this as a diagram, the resulting figure is called a graph. Price varies and so does time, but there is a relationship between them. In any case, where two facts capable of being expressed numerically are related in such a way that for a value of one there is a corresponding value of the other, we are in a position to plot the relationships on paper and produce a graph. This principle is made use of in business, and we are able to record by graphical representation the relationship of manufactured product to raw materials, gross profit to revenue, turnover to successive financial periods, and numerous other relationships much in the way that the barometer readings are charted at our meteorological observatories.

Graphs are usually prepared on squared paper, and the first step is to set up a frame work from which to commence operations. A horizontal line OX is drawn at the bottom of the paper, or one of the horizontal lines on the paper is selected. Similarly a vertical line OY . These are known as the axes of reference, and the point O is called the origin, usually the zero point. (See diagram, at top of next column.)

Suppose potatoes cost, during twelve months in a given year, the following number of pence per lb.—

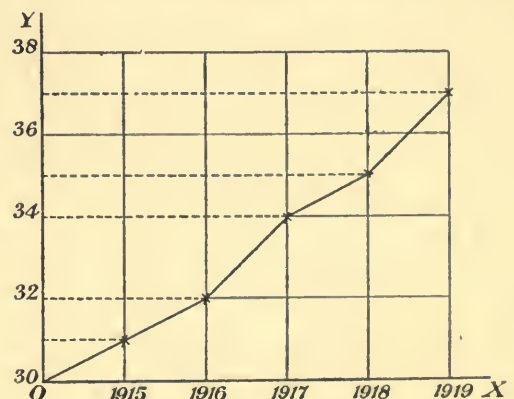
	d.		d.
Jan. . .	$1\frac{1}{2}$	July . .	5
Feb. . .	$1\frac{3}{4}$	Aug. . .	$3\frac{1}{2}$
Mar. . .	2	Sept. . .	2
Apr. . .	2	Oct. . .	$1\frac{1}{2}$
May . .	$2\frac{1}{4}$	Nov. . .	$1\frac{1}{2}$
June . .	6 (new)	Dec. . .	$1\frac{1}{2}$

We relate price to time by setting out along OX the twelve months and along OY the pence. The highest price is 6d. and the lowest $1\frac{1}{2}$ d.; the highest month is the twelfth and the lowest the first. Let each square represent 1 unit in each case. The price in January is represented by a



vertical line $1\frac{1}{2}$ squares high at point 1 in OX . The price in February by a line $1\frac{3}{4}$ squares high at point 2; the price in June by a line 6 squares high; and so on. Draw these lines and join the tops by means of a thin continuous line, and we have a graph of prices for potatoes for twelve months. It will be seen that the vertical lines may be neglected, as we have the graduated axis OY to refer to. This is very simple, but it is the basis of *all* graphical representation.

In more complicated exercises, and indeed in most graphs familiar to accountants, it would not be possible with the figures used to indicate zero on the diagram. In such case, the vertical lines erected at the points on OX will not represent the figures used, and so will have no significance; thus if we are tracing prices ranging from 30 pence to 36, it is not necessary to show values below 30. The point O may therefore be 30, in which case values less than 30 are below the line OX ; that



is, for our purpose and the convenience of drafting, the line OX may slide vertically along OY, and similarly OY horizontally along OX, as in the figure on the previous page.

The chief value in a graph is that it is a simple matter to glance along its curve to note irregularities and to forecast probable tendencies in business from the trend of the curve, *i.e.* from its general direction and slope over a period of time.

Diagrammatic representation does not add to the meaning of figures, but is useful (1) for comparison of groups similarly related, *e.g.* comparison of elements of cost per unit of output for manufacture under varying conditions; (2) for comparison of costs for successive financial periods, *e.g.* wages of production weekly or produce—*i.e.* units of output weekly.

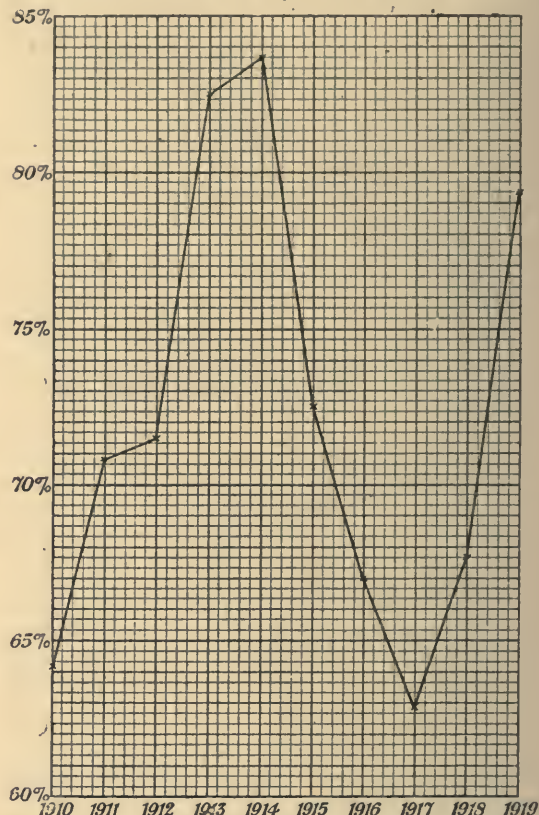
It is not wise to dogmatise on the subject of diagrams; representation by this means appeals with different degrees of force to different persons, and a statistical diagram should be rejected if it fails to help the investigator to visualize the statistics under consideration.

The test of a diagram is its legibility and clearness. It should carry on its face the meaning of the facts represented. Multiplicity of lines is fatal. Lines, if in number, should be distinguished by colours. Where there is much detail to consider, diagrams are useless unless the "data" can be shown in separate diagrams. If the "data" is not divisible, it will be easier to deal with it as a table than in graphic representation.

Under no circumstances should diagrams be made merely for the sake of framing charts. Unless a diagram renders the statistics clearer, the statistics should be allowed to stand on their own merits.

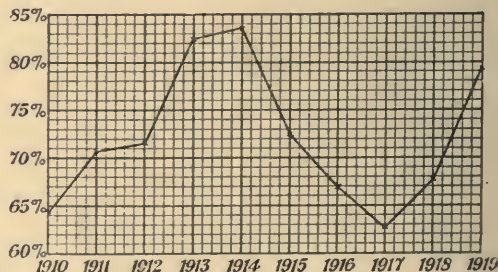
For the purpose of accurate representation, care should be taken in choice of a scale, since, unless a scale really appropriate is selected, a graph may be made to accentuate facts or minimise them, and in either case they become unreliable. In order to choose an appropriate scale, it is necessary to consider the range of the graph. Suppose we are depicting percentages, say, of working expenses to revenue, the upper limit must be less than 100, or the business is doomed. The lower limit may be anything below 100 (see Table on page 880), say, 60 lowest and 85 highest, the range being 60 to 85 or 25 units. Our graph must admit of 25 units. Suppose the paper at our disposal is divided into tenths of an inch and is 8 in. long, there are 80 squares available: $80 \div 25 = 3$. We can afford 3 squares to each unit. The number of years is 10, and the paper 5 in. wide or 50 squares, giving us 5 squares to the year. One square would be cramped, whilst five is satisfactory. The diagram of percentages from the table given in statistics may be plotted on the scale 3 to the inch vertically and 5 horizontally.

The graph is plotted as follows: 1910 is at the point 0. Vertically above, mark the appropriate percentage 64.5; above 1911, mark 70.7, and so on; then join up the points as shown.



Now let us adopt the scale 1 square to 1 unit of percentage, and proceed as before; then compare the two diagrams. The second one in the writer's opinion discloses most fairly what has taken place. If the vertical scale is unduly small, the diagram flattens out and hides what is taking place.

In plotting revenue from the same table, the



COSTS PER TON OF TRINITRO-TOLUENE IN 6 FACTORIES.

Costs per Ton of T.N.T. made.	TOTAL £104-787						TOTAL £97-792						TOTAL £93-387						TOTAL £87-748					
	GENERAL £3-175	MAINTENANCE £5-169	LABOUR £4-518	GENERAL £7-451	MAINTENANCE £9-848	LABOUR £7-178	GENERAL £1-76	MAINTENANCE £5-69	LABOUR £2-90	GENERAL £3-261	MAINTENANCE £3-008	LABOUR £3-417	GENERAL £7-066	MAINTENANCE £4-422	LABOUR £2-706	GENERAL £2-561	MAINTENANCE £5-026	LABOUR £4-616	GENERAL £4-043	MAINTENANCE £5-103	LABOUR £2-412	GENERAL £1-76	MAINTENANCE £3-008	LABOUR £2-90
£110																								
£100																								
£90																								
£80																								
£70																								
£60																								
£50																								
£40																								
£30																								
£20																								
£10																								

TOTAL PRODUCTION
25,482 TONS.

FACTORY A. FACTORY B. FACTORY C. FACTORY D. FACTORY E. FACTORY F. AVERAGE. BOGEY.

Costs per Ton per Factory

Bogey = Total costs made up of lowest costs of each element in all factories

range is from £81-608 to £35-031, or roughly through £46-000; on 8-in. paper with 80 squares this sum is to be represented. If the working expenses are to be shown on the same chart, the lowest figure is £23-687; and if gross profits are to appear, the lowest figure is £11-344, or a range of £81-608 to £11-344, roughly £70-000; each square could represent £1-000. It would be impossible to indicate units and tens on such scale, and to obtain a reliable graph in the space available the nearest £250 could be depicted (*i.e.* quarter of a square). Proceed, first, to approximate all figures to the nearest £250, and with the new set of figures proceed to plot: thus, in 1910, 11-25 units' gross profit, 23-75 units' expenses, and 35 units (thousands) revenue. Plot the three curves, and note that such a diagram does not transgress the rules as to clearness, as none of the lines cross.

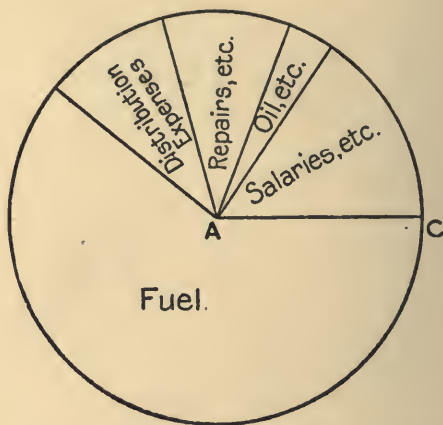
Before drawing a graph, make the necessary calculations, leaving plenty of margin for rise and fall, as some of the figures are in the future and cannot be anticipated. Graphical representation is suitable to the study of *series* of variables. For comparison purposes, areas are used for diagrammatic representation; but for the most part, such diagrams are pictorial only, and little time should be spent in their preparation, unless in a simple form directed towards advertisement. The circle is sometimes used to represent total cost or sales. This is divided into segments to represent component costs and profit. Consider the following table of costs—

Fuel	£	17,000
Oil, Waste, Water, and Stores		950
Salaries and Wages		4,450
Repairs and Maintenance		2,750
Works Cost		25,150
Distribution Expenses		2,500
Total Generation and Distribution Costs	£27,650	

The whole circle would represent £27-650. We now proceed to divide it into its components. The area of a segment is proportional to the angle of the segment, so that the whole area is proportional to 360°. Half the area has an angle $\frac{1}{2} \times 360^\circ = 180^\circ$; $\frac{1}{3}$ has an angle $\frac{1}{3} \times 360^\circ = 120^\circ$. In the table, Fuel costs £17-000, and would represent $\frac{£17-000}{£27-650}$ of the whole circle, the angle of the segment having this area is $\frac{340}{553} \times 360^\circ = 220^\circ$ to nearest degree.

Draw radius AC and mark off 220°, thus making the segment representing fuel. Proceed with each component and complete the diagram.

For purposes of comparison, the circle is not so useful, and it is found that rectangular figures are more convenient. By keeping bases constant and allowing rectangles to vary only in height, comparisons can be easily made. Considerable expense has been incurred in the costing of Government factories on preparing such diagrams for what they are worth.



The chart on page 883 is self-explanatory, showing the diagrammatic representation of the costs of production per ton of Tri-nitro-toluene in six Government factories, together with a composite diagram of average costs and a diagram (bogey) showing the cost, taking the lowest figure for each element in the various factories.

STATUTE-BARRED DEBTS.

A debt is said to be statute barred when, by the Statute of Limitations, 1623, a period of six years has been allowed to go by and nothing has been done by the debtor to keep it alive. This applies to a simple contract debt. If the debt is a specialty debt, that is, one arising out of a contract under seal, the period is twenty years instead of six years. The Statute bars the right to sue; it does not otherwise affect the validity of the contract. Thus, if a tradesman supplies goods, and brings an action for the price of the same seven years later—nothing having been done in the meantime—he can make good his claim, if he proves the delivery of the goods and the prices charged are fair and moderate, unless the defendant specially pleads the Statute of Limitations. Should the defendant fail to set up this statutory plea in his defence—or give notice of the same if the case is tried in a County Court—he will not be heard upon the point at the trial of the action. As further illustrating this peculiar position, it is to be noticed that an executor is fully justified in paying a debt incurred by a testator, even though

the company, the report must be certified by the sole director or manager. Further, that part of it which relates to the allotment of shares, cash received for shares, and receipts and payments on capital account must be certified by the auditors. Unless the company is a private company, a copy of the report must be filed with the Registrar after it has been sent to those entitled to receive it.

The Act requires that at the commencement of the meeting there must be produced a list of members, showing their names, addresses, and descriptions, and this list must remain open and accessible to any member during the meeting. Although the meeting is at liberty to discuss any matter relating to the formation of the company or arising out of the report no resolution may be passed unless previous notice of it has been given. If necessary, the meeting may be adjourned from time to time. It is not competent for the company to vary the terms of any contract referred to in the prospectus before the statutory meeting takes place, unless the variation in the contract is subject to the approval of the statutory meeting. Although the statutory meeting is a general meeting, it is not regarded as an ordinary general meeting for the purpose of Section 26 of the 1908 Act, which requires the filing of the Annual Return and Summary. Consequently, a return under this section is not required after the statutory meeting. As there is considerable misunderstanding on this point, the following, which is a copy of a letter received from the Registrar of Joint Stock Companies, is of interest—

"This office does not recognise a statutory meeting as an ordinary general meeting under any circumstances. There has not been, so far as I am aware, any decision on the point, but it is assumed that the return of allotments, and in the case of a company which is not private the statutory report, give shareholders all the information at the disposal of the company at the early period in its existence represented by the statutory meeting."

The failure to hold this meeting is a ground for winding up by the company, but, instead of ordering a winding up, the Court may order the meeting to be held. In conclusion, it may be

stated that the notice convening this meeting should indicate clearly that it does refer to the statutory meeting, and must be given in accordance with the regulations contained in the Articles, though the fact must not be overlooked that the Statutory Report must be sent out at least seven clear days before the meeting.

STATUTORY REPORT, AUDITOR'S CERTIFICATE ON.

(See AUDITING, p. 70).

STOCK.

In many businesses it is important to keep exact particulars of each class of stock held, in order to control the stock and to obtain a check against fraud.

In dealing with trading stocks, the method adopted in all businesses where leakage may take place is that of keeping accounts in debit and credit form. The accounts, of which one is provided for each line dealt in, vary in particulars to meet the requirements of each special business, and the forms given instance those of a jeweller, a draper, and a woollen merchant.

The accounts are debited with goods manufactured, or purchased, and are credited with those sold, the balance agreeing with the stock actually in hand at any time. Allowance is made for cutting off, weighing out, etc., to such extent as is found by experience to be the usual amount of loss.

Such accounts not only give absolute control over each stock in hand, so that any running short may be replaced, and prevent fraud, but it may be seen at once which "lines" have the best sale, and their increase or decrease in popularity may be followed.

A similar method is adopted for stocks used in manufacturing, but here the Stock Books are known as Stores Books or Stores Ledgers, the debits being made from the Stores Received Book, entered from the invoices on purchase of the goods, and the credits from the Stores Issued Book, the latter being written up from issue orders. Examples of Stores Ledger Accounts are given in this article—

JEWELLER'S STOCK BOOK

No.	GOLD RINGS.		Date.	Price.	Remarks.	No.	Date sold.	Amount.	Cash Book or Day Book Folio.	Remarks.
	Description.	From whom Purchased.								

DRAPER'S STOCK BOOK

Stock No.	Invoice No.	Length.	Particulars.	Per yd.	Invoiced Amount.	USED.				RETURNED.			
							Total yds.	A	ount.	Date.	Length.	Debit Rns. Bk.	Amount.
					£ s. d.	O/Nos.			s. d.				£ s. d.
						Length							
						O/Nos.							
						Length							
						O/Nos.							
						Length							

WOOLLEN MERCHANT'S STOCK BOOK

Piece No.	Selling Price.	Pattern No.	Date Received.	Manufacturer's Name and Address.	Manufacturer's			Length.	How Disposed of.		Order No.	Length.	Price.	Remarks.
					Piece No.	Pattern No.	Cost Price.		Date.	Name.				
160	3/9	61	Feb. 2	Joseph Medland & Co. Victoria Street, Manchester	19680	350	2/4	52 1/4	Feb. 4	H. Stubb, Ltd.	10	5	3/0	
								51 1/4	" 8	F. Davies & Son	56	8	2/9	
									" 10	B. Southern & Co.	9	2 1/2	3/-	
									" 20	W. Meeson, Ltd.	3	14	3/0	
									" 22	H. Goodman	21	12	2/8	
									" 27	S. Terry & Co., Ltd.	72	10	13/0	
					Total			51 1/4				51 1/4		

ENGINEER'S STORES LEDGER

STEAM TUBES

	No.	T.	C.	Q.	Lb.	Price.	£ s. d.		No.	T.	C.	Q.	Lb.	Price.	£ s. d.
Dugdale Iron Co.	11	5	0	0		£10	112 10 0	Issues	3	10	0	0		£10	35 0 0
Consett Iron Co.	3	0	0	0		£9 10s.	28 10 0	"	2	10	0	0		"	25 0 0
								"	3	0	0	0		£9 10s.	28 10 0
								"	5	5	0	0		£10	2 10 0
								Stock carried forwd.	5	0	0	0		"	50 0 0
	14	5	0	0			£141 0 0		14	5	0	0			£141 0 0
Stock brought forwd.	5	0	0	0		£10	50 0 0								

5" x 3" x 7/16" ANGLE BARS

	No.	T.	C.	Q.	Lb.	Price.	£ s. d.		No.	T.	C.	Q.	Lb.	Price.	£ s. d.
Lloyd & Stott	20	0	0	0		£10	200 0 0	Issues	2	0	0	0		£10	20 0 0
								"	7	0	0	0		"	70 0 0
								"	4	0	0	0		"	40 0 0
								Stock carried forwd.	7	0	0	0		"	70 0 0
	20	0	0	0			£200 0 0		20	0	0	0			£200 0 0
Stock brought forwd.	7	0	0	0		£10	£70 0 0								

those of past periods, inflations of values giving swollen profits, and under estimation of values creating secret reserves.

In the case of stock for which there is no possibility of ready sale, or "dead" stock, this should be noted on the stock sheets and taken at a depreciated figure not greater than that which it would probably realise if sold on the date of stocktaking.

It must be borne in mind that profit is not earned until goods are sold, and, therefore, should the market price at the moment of stocktaking be higher than that given for the goods, as there is no assurance that it will be maintained, profit should not be anticipated by advancing the value to that figure. In regard to goods purchased for re-sale, safety lies in following the recognised rule, and valuing at cost price or present market price, whichever may be the lower, inward carriage and work done which has added to the value being, of course, taken as part of the cost.

The valuations of stocks on hand in manufacturing businesses should be made on the following basis—

(a) **Finished Goods.** The cost of raw materials, plus the cost of manufacture, providing such a total cost does not exceed the current selling price of the goods. In the latter case, the utmost value which could be taken would be such selling price.

(b) **Partly manufactured goods.** The cost of raw material, plus the cost of such partial manufacture.

(c) **Raw materials.** The cost price or the current market price, whichever may be the lower, adding direct charges.

In the cases of wine merchants, timber merchants, and others whose stocks mature by keeping—the longer they are kept the more they appreciate in value—a percentage is added to the original cost of stock, as interest on the capital sunk in the stock, as is also the cost of storage.

STOCK ACCOUNT.

(1) An account kept for each class of article used in manufacture or dealt in by way of trade, the account being debited with the quantity purchased, and credited with the quantity issued or sold, the balance at any time thus agreeing with the stock actually in hand.

(2) An account kept for the reception of the total of the stock at each periodical stocktaking, the Trading Account being credited and the Stock Account debited. The account is closed on next balancing by crediting the Stock Account and debiting the Trading Account.

STOCK ACCOUNTS, APPROXIMATE.

Accounts kept in order to give the approximate stock in hand without the trouble of stocktaking,

and raised by adding to the amount of the last stock purchases since made, and deducting returns and the estimated cost of goods sold, the latter being arrived at by deduction from the selling price of the gross profit which it is anticipated is being made by knowledge of past results, and having regard to any factors which may be likely to cause any fluctuation.

STOCKBROKER'S ACCOUNTS, AUDITORS AND.

(See AUDITING, p. 115.)

STOCK IN HAND.

(See AUDITING, p. 79.)

STOCK-IN-TRADE.

The accuracy of the quantities and valuations of goods in stock has an important effect on the ascertainment of true trading profits.

Stocks should be taken by the persons in charge thereof, checked by other responsible officials, and priced by the managers. The calculations should be made by one clerk and checked by another, and each person taking part in the work should sign the stock schedules for the duty he has undertaken.

The following general principles should be adopted in the valuation of stock, viz.—

Raw materials, and goods sold in the form in which they are purchased, should be taken at cost or market price, whichever is the lower.

Work in progress should be valued at the cost of the original raw materials plus the labour expended upon them to the date of stocktaking.

Finished work should be valued on the same basis as work in progress, plus the further addition of a proper proportion of general establishment expenses. In some cases it is customary, and perhaps permissible, for finished stock to be taken at a price which includes a proportion of profit, where such profit is assured; but, as a general rule, this practice should be discouraged, and, in any event, the cost of carriage outwards and other expenses of dispatch and distribution, including general establishment expenses, should be deducted.

The auditor's duty as regards stock is to satisfy himself that it fairly represents the value of the goods on hand. He is entitled to rely on the certificates of properly authorised officials. The fact that he has done so should always be reported to the shareholders. He should, however, not merely content himself by accepting such certificates, but should verify the prices at which the stock is taken by reference to previous stock lists and by comparison with the invoices for goods purchased. He should furthermore test a good proportion of the calculations, and should check all the additions, which are a common source of

error. In addition to this, it is his duty to ascertain, as far as is within his power, that all invoices for goods which have been taken into stock are included in the charges against the revenue of the period. (See also ACCOUNTS, CRITICISM OF, p. 14; AUDITING, pp. 79 and 95; BALANCE SHEET, p. 152; LIQUIDATORS, ACCOUNTS OF, p. 648; STOCK ACCOUNTS, APPROXIMATE TRADING ACCOUNT, p. 95.)

STOCK LEDGER.

(See STORES AND STOCK RECORDS AND ACCOUNTS, p. 902).

STOCK RECORDS AND ACCOUNTS.

(See STORES AND STOCK RECORDS AND ACCOUNTS, p. 896.)

STOCKTAKING.

The expression stocktaking is commonly used to denote the taking of stock for the purpose of the annual balance sheet and accounts of any undertaking as distinguished from a valuation of stock for the purpose of realisation in a liquidation or bankruptcy, or for probate. Stock enters into the annual accounts in two ways. It is included in the balance sheet as an asset of realisable value and is therefore a factor in estimating the financial position. It also appears in the Trading Account, in which, as a rule, the stock at the beginning of the accounting period to which it relates is the first, and the stock at the end of the period the last item, the latter being the first item in the Trading Account of the succeeding year and so on from year to year.

METHODS OF VALUING STOCK.—Unless the stocks be taken from year to year on the same basis, it is clear that a true and correct Trading Account cannot be raised. An inflation in one year means an anticipation of profit in that year, to the detriment of the following year. For example: If at the end of 1920, stock was valued at selling prices (these being assumed to be above cost price, as it would usually be in the case of a profitable concern) the profit on sales in 1921 out of that stock would have been anticipated. The profits of 1921 would be correspondingly reduced, and the expenses of that year borne solely out of profits on sales of stock not in hand at the beginning of the year. If the quantities of stock from year to year were continuously increasing, and systematically over-valued, the effect of over-valuation in the early years on the profits of the succeeding years would not be so marked, but as soon as the quantities began to decrease, the effect of the over-valuation would be severely felt. For these reasons it is essential that stock be correctly enumerated and fairly valued from year to year.

In the case of manufacturing concerns the value of raw materials should be based upon the average

cost of the material bought during the year; the value of work in progress and finished stock is based upon the cost price as shown by the Stock Accounts, subject always to the reservation that this does not exceed market price. Scrap material, which is continually being cleared out, does not, as a rule, present a serious problem, and its value is governed by what it may be expected to fetch.

Stocks of loose tools and plant usually form a separate item in the Balance Sheet, and the stock-taking of these items is intended as a check upon their book value. Stocks of this description should be severely depreciated at each stocktaking.

In certain trades where the raw material and the finished product are subject to wide fluctuations in price, the practice prevails of taking the stock at current market rates (provided it is not earmarked to contracts at agreed prices) even although above or below cost. If the stock does not vary greatly in quantity from year to year this will, on an average, work out fairly, due reserves being made in exceptional cases where a fall in price is anticipated. This is on a par with the practice of Stock Exchange firms who bring stocks and shares into their accounts from settlement to settlement at the make-up prices in the market.

The principle upon which stock is generally valued for stocktaking purposes is expressed in the form of certificate required to be appended to the stock sheets each year for the satisfaction of the auditor.

Certificate as to Stock.

I hereby certify that the above is a correct list of the stock as at _____ 1st _____ amounting in value to £ _____ that same has been taken at cost price or at market value if lower, and that due allowance has been made for old, damaged and depreciated goods.

Quantities taken by _____

Prices and proper allowances fixed by _____

Moneying out and additions made by _____

Checked by _____

Finally approved by _____

I further certify that the said stock-in-trade was the property of the Company on the said date and was then in its possession, and that it includes no plant, machinery, fixtures or fittings.

Signed _____

(General Manager or other responsible Official.)

If the principles embodied in the certificate (as above) be adopted then, so far as stock is concerned, the Balance Sheet is sound, and the Trading Account reliable.

Methods of Stocktaking (Enumeration). As to the taking of retail stocks, the subject is dealt with under the heading of "Methods of Stocktaking"

in the article on DEPARTMENTAL STORES (p. 388), to which the reader is referred.

The methods adopted in the great wholesale and distributing houses are of a similar nature, and do not present any exceptional features.

It only remains to describe the methods adopted in manufacturing concerns where there are stores, raw material and work in progress, as well as finished stocks to be considered, the stores and work in progress being scattered through many shops and departments, and more or less in a constant state of flux.

The following regulations as to stocktaking are those followed in a highly organised modern factory, and they serve as an illustration of up-to-date stocktaking.

STOCKTAKING ROUTINE.—Symbols. Each of the departments or divisions is symbolised by an alphabetical letter.

Every item in the Standard Trading Stock is symbolised by a letter and numeral, the former preceding the latter. The letter so allocated is that of the department or division to which the item belongs, and the numeral one of an allocated series, as under.

The symbol thus allocated is posted in the index of a "Stock Record."

In order to prevent possible confusion, care is taken that any pattern numbers or marks that may be required to be stamped or cast on patterns or material, conform to the stock symbol allocated to such pattern or material. In order to obtain distinctive series of numbers for the different classes, each series commences at least 100 in advance of the first number of the preceding series, as shown in the following Table of Symbols allocated to each department or division—

Departmental Symbols.	Series of Items.
Apparatus for Treating Liquids A	1,000 to 1,999
Glass B	2,000 " 2,999
Crystals C	3,000 " 3,499
Acids D	3,500 " 3,749
Packing Goods E	3,750 " 3,999
Fire Extinguishers F	4,000 " 4,499
Terminals G	4,500 " 4,999
Hard Metal Castings H	5,000 " 5,999
Tyre Inflators I	6,000 " 6,499
Beer Extractors J	6,500 " 6,599
Gaskettes K	6,600 " 6,699
Woven Mesh M	6,700 " 6,899
Experiments N	6,900 " 6,999
Home Advertising O	7,000 " 7,499
Foreign Advertising P	7,500 " 7,749
Subsidiary Lines, advertising Q	7,750 " 7,999
Pictures, advertising R	
Stationery S	8,000 " 8,999
Universal Stores U	9,000 " 9,999
Metals and Alloys V	10,000 " 10,199
Heat, Light and Power W	10,200 " 10,399
Scrap Materials X	10,400 " 10,599

Stock Labels: All the bags, bins, shelves, and other receptacles for stock in the stores and elsewhere in the works are symbolised in like manner to that described above, by means of a printed and eyeletted label, which is framed or nailed or tied to a receptacle as may be most convenient; by this means the nature of the contents of such receptacle is displayed by symbol and description, whereby the symbols may be the more easily introduced, remembered, and applied by the staff generally.

Teller's Tallies: Before 30th November, each year, "Tellers' Tallies," numbered from 1 upwards, bound in volumes containing 250 pages in each, each page being perforated for tearing from a counterfoil, are ordered and obtained.

Draft Stock Sheets: Before 30th November, each year, "Draft Stock Sheets" of suitable size for ruling and printing are ordered and obtained. These draft stock sheets have spaces for the various particulars (symbols, location, operation, quantity, weight, price per unit and stock value). "Stock Record Sheets" are ordered and obtained and printed in such a manner that they can afterwards be bound face to face with the pages containing the same items in the previous year's stocktaking for purposes of comparison.

On or after 1st December, but not later than 21st December in every year, the "value per unit" is ascertained or determined of every item known or believed to be in stock at the time, and such value is posted to the Draft Stock Sheets in preparation for the forthcoming stocktaking, and the supervisor under whose supervisions these sheets are being prepared, asks for and obtains the initials on the Draft Stock Sheets of the manager or managers responsible for fixing such value, and who will be called upon at the conclusion of stocktaking to sign the usual Stock Certificate.

[NOTE: The simplest manner of doing this is for the manager responsible to either confirm or amend the value per unit on the Draft Stock Sheets used at the previous year's stocktaking.]

Before 15th December in every year, the persons required by the management to be engaged in the next stocktaking, viz.: "Tellers" and Labourers, are informed of the dates on which their services will be required, and before 21st December the Tellers are instructed in this system and their duties thereunder.

In order to secure uniformity of method, the direction of the process of stocktaking is entrusted entirely to the Stocktaker-in-Chief, hereinafter referred to as the "S. C."

Early in the month of November in each year the S. C. inquires into and satisfies himself that the necessary special stationery for stocktaking is in existence, or on order.

Early in December in each year the S. C. inquires into and satisfies himself that the preliminary work required to be done as described above, is being carried out.

Between 1st and 21st December the S. C. visits the works on one or more occasions as required in order to ascertain if the "Stock Labels" are in position as required and accurately filled in. He also ascertains the names of the Tellers appointed for the forthcoming stocktaking, and satisfies himself that they understand the duties required of them, and are intelligent and willing.

Commencement of Stocktaking: On 28th December in each year, or such other date as the Directors may appoint, the S.C. Tellers, and Labourers having assembled, and the S. C. being in possession of the "Stock Record," "Draft Stock Sheets," "Tellers' Tallies," and "Stock Indices," the S. C. shall give to *each* Teller a Tally Book and Stock Index with instructions as to the order in which he is to proceed in his respective department; and a typed copy of the following regulations shall be placed in an accessible position for reference by the Tellers.

Stocktaking Regulations: Rules—

(1) The Tellers shall observe and carry out the requirements of the S. C. in all things during stocktaking and refer to him any doubtful point requiring an explanation or decision.

(2) The Tellers shall commence to record the stock in the various departments at a spot in each selected or approved by the S. C., and the order of commencing and proceeding shall be for the goods nearest to the aforesaid spot to be first recorded; and next in order the nearest goods to those first recorded, and so on until every item in such department or departments has been recorded in the manner described below.

(3) The Tellers shall not themselves handle any goods (except by way of checking the goods in process of being counted or weighed by the labourers provided for that purpose), but shall confine their attention strictly to counting or weighing, or to checking the counting or weighing, of goods; and to recording the quantities of each item so ascertained in a neat and clean manner on the tallies provided, using the symbol allocated wherever possible, and only describing in longhand goods which are of recent introduction and so as yet unsymbolised.

(4) A Teller shall, after correctly recording on a tally and counterfoil the goods last counted or weighed, affix such tally to the goods, or to the floor or wall near by, in such a manner that it cannot be disturbed, or be confused with other goods in the same environment; and so that it shall be *clearly visible* to the S. C. at a reasonable distance.

(5) A Teller having affixed a tally in position,

shall not amend or remove it without the permission of the S. C.

(6) A Teller shall not destroy any of the said tallies, no matter whether spoiled or not: but shall preserve all spoiled tallies and hand them to the S. C., so that the tally may be found to be missing at the conclusion of stocktaking, and so that no question shall afterwards arise as to the value of a missing tally.

(7) A Teller shall not count or weigh or watch the counting or weighing of more than one item at one time, or proceed with the recording on more than one tally at the same time: that is to say, that until the last tally has been affixed in position there shall be no writing whatever on any other tally or counterfoil still in the Tally Book.

(8) A Teller shall not record more than one item on any tally; or, even two quantities of the same item on the same tally, if such quantities be separated in any manner likely to lead to confusion as to the separate quantities recorded. Exceptions to this rule should only be made with permission of the S. C.

(9) A Teller shall, upon completing the recording of all goods in the department or departments to which he has been deputed, report the same at once to the S. C.

(10) The S. C. may from time to time during the performance of the Tellers' duties, make certain tests of their accuracy; and it shall be understood that such tests are without suggestion that those duties are not being properly and satisfactorily performed.

Completion of Stocktaking: (12) Upon the S. C. being satisfied by observation that the whole of the stock in any department has been counted or weighed and correctly recorded, he may then commence—

(a) to collect or cause to be collected by the Tellers or others, the whole of the tallies affixed as aforesaid.

Time allowed— $4\frac{1}{2}$ days.

(b) The tallies when collected shall be conveyed to the S. C.'s room, and there be dealt with in the following manner—

The tallies shall be placed in proper numerical rotation according to their tally Nos., including all spoiled and cancelled tallies, and shall be placed in bundles of 250 each, corresponding to the Tally Books, and such bundles be securely tied or otherwise fastened.

The S. C. shall then ascertain that every tally torn from the Tally Books has been collected and returned to him, and if any be missing he shall cause a search to be made for same until found or accounted for.

Time allowed—3 days.

(c) The bundles having been arranged and checked as described above, shall then be broken

and the tallies re-arranged in the numerical order of the symbols, which process will automatically classify the items into their respective departments and allocated order in such departments, except such tallies as may represent goods recently introduced and as yet not symbolised. The descriptions of such goods shall be thereupon alphabetically arranged and symbols allocated thereto. The new symbols shall at once be added to the tallies, and the tallies be placed in their proper symbolical order.

(d) Gas, water, and steam piping; cast and mild steel; iron and brass; files, belting and sundry engineer's stores may at the direction of the S. C. be recorded in one or several lists (which lists shall be priced, and the particulars, quantity, average price, and total value recorded *in ink* on a master-tally, or tallies, which shall afterwards be placed in its proper symbolical order).

Where more than two tallies are symbolised alike a master-tally shall be prepared in ink and affixed to such tallies; and the master-tally shall, on the back of it, have recorded the quantity recorded on each tally together with the tally number, and on its face shall carry the total quantity represented.

(e) The symbols, quantities, processes, and location shall then be posted from the tallies to the Draft Stock Sheets, at the completion of which the tallies shall again be tied or otherwise fastened together and labelled departmentally, and in this form be carefully stored for reference if required, until the following year's stocktaking is completed, when they may if desired be destroyed.

Time allowed—5½ days.

Completing Draft Stock Sheets.

(f) The Draft Stock Sheets will next require the addition of certain "values per unit" added for goods found in stock and recorded but which were not anticipated at the time of preparing these sheets: after which they shall be extended in the usual manner (q.v.t.) and the additions made for the totals to be carried to the summary.

q.—Quantity of Items.

v.—Value of Unit of Item.

t.—Total value of Quantity of Item.

Time allowed—5½ days.

Abstract to Stock Record.

(g) When the S. C. is satisfied that the Draft Stock Sheets are complete and correct, the required Abstract shall be posted therefrom to the Stock Record, after which a stock certificate in the terms required by the company's auditors for the time being, shall be added at the foot of the stock summary at the end of the said stock record, and the same be signed by the said S. C.

Time allowed—2 days.

(13) The S. C. shall exercise, and be allowed to exercise his discretion in ascertaining the accuracy of all stages of the procedure, in view of the certificate required of him.

(14) The S. C. should, before the conclusion of his work, make a note of the amount of special stationery used during stocktaking, the amount remaining in hand unused, and the amount of new (if any) required to be ordered before the next stocktaking, and request the secretary to order forthwith any new stationery that may be required, so that the means for taking stock may be ready for use at any time required.

(15) By the adoption of this system it should be possible to learn the value of the asset "Stock-in-Trade" by the 21st January in each year, and to see the result in a comparative form with the results of the previous year before the end of the same month. This enables the company's Balance Sheet to be issued on the 31st of January in each year if so desired.

VERIFYING QUANTITIES.—In cases where total quantities purchased and sold, or quantities of raw material bought and quantities of output can be readily ascertained, it is possible closely to test the quantities of stock which ought to be in hand with those shown to be actually in hand by the stocktaking, due allowance being made for evaporation, waste, etc. This applies, for example, to such diverse trades as the manufacture of cocoa, brewing, and detinning of tin scrap. (See DEPARTMENTAL STORES, p. 387.)

STOCK VALUES.

(See INVESTIGATIONS, p. 575.)

STOCK, VERIFICATION OF.

The item of stocks in balance sheets claims more than passing consideration seeing how comparatively easy it may be in some cases to manipulate it with the object of endeavouring to conceal fraud or inflate profits. Much has been written on the subject, and so far as the auditor's duty and responsibility are concerned, the legal requirement is that he (the auditor, whose duty is to the shareholders, the directors being simply trustees and executive of the members) must exercise reasonable care, diligence, and skill, and that subject thereto, he is not responsible for any designing schemes of fraud. As to the interpretation of reasonable care, diligence, and skill, each case must be considered in the light of the particular circumstances.

In what is known as the *Kingston Cotton Mill* case, which dates back to 1895, the Court of Appeal per Lindley (L.J.) delivered itself thus: "For several years frauds were committed by the managers who, in order to bolster up the company, and make it appear to look flourishing when it was the reverse, deliberately exaggerated both the quantities and values of the cotton and yarn in

the company's mills. He did this at the end of the years 1890, '91, '92, and '93. The balance sheets of each year contained on the assets side entries of the values of the stock-in-trade at the end of the year, and these entries were stated 'as per manager's certificate.' The auditors did not profess to guarantee the correctness of this item of stock-in-trade. They assumed no responsibility for it. They took the item from the manager, and the entry in the balance sheet shows that they did so. I confess I cannot see that their omission to check his returns was a breach of their duty to the company. It is no part of an auditor's duty to take stock. No one contends that it is. He must rely upon other people for details of the stock-in-trade. But although it is, no doubt, true that such a process might have been gone through, and that if gone through, the fraud would have been discovered, can it be truly said that the auditors were wanting in reasonable care in not thinking it necessary to test the manager's returns? I cannot bring myself to think that they were, nor do I take a different view."

Lopes (L.J.) in the course of his remarks on the same case stated "that it was the duty of the auditor to bring to bear upon the work he has to perform that skill, care, and caution which a reasonably competent, careful, and cautious auditor would use. What was reasonable skill, care, and caution must depend upon the circumstances of each case."

As an example, take the detailed balance sheet of a business in which the following items occur—

- (1) Stores and materials and articles to be consumed or utilised in production;
- (2) Manufactured stock-in-trade, that is, manufactures completed and available for sale;
- (3) Manufactures in progress of completion at the date of the balance sheet.

The auditor's precise duties, apart from those of the usual orthodox nature, will depend more or less upon the soundness of the accounting methods in practice, and the practical value of any system of internal check which may be in vogue. The salient objectives are quantity and value. It is of the utmost importance that he should assure himself by every possible means or device that all purchases delivered have been brought into account, and properly brought into account, for the purpose not only of arriving at the true liabilities, but of pursuing and confirming the disposition of the purchases.

When performing the audit, it is well to take entries which have been made for the ensuing year and inspecting cursorily the invoices and statements with a view to satisfying oneself as far as possible that they have been treated in the proper year's accounts. All goods delivered should naturally be embraced in the accounts of that year, and all goods invoiced but not received until

the ensuing year may be credited to the various supplies concerned and debited to a goods in transit account.

With regard to the entries under class 1—stores and materials to be consumed for the most part in manufacture or production—these would probably appear in the ledger account under the general heading of stock of consumable stores, the purchases being posted thereto, say, in monthly totals. Should there be a costing department with a proper system of costing, the issues from such stock would be periodically credited thereto and debited to the costing department or some other account, to be accounted for in saleable stock. Included in the subsidiary set of books kept by the costing and stores departments, there would be a Stores Ledger, a Stores Received Book, and a Stores Issued Book, the Stores Ledger perhaps being kept by the costing department, and the Stores Received and Issued Books by the storekeeper. Suitable accounts in the ledger would be raised to which the entries in the received and issued books are posted, the details for the latter being obtained from advice of goods received and passed, and the issues from the executed requisitions, goods being only supplied or issued on the production of requests or requisitions properly authenticated. It will thus be seen that the total of the various balances of the accounts in the stores ledger should agree with the balance of the accounts in the counting-house ledger, subject to allowances for inherent differences and the necessary adjustments. There are, however, undertakings in the making of which there is no such system as we have briefly sketched, in practice, or, indeed, any system adequate to their primary need; but the absence of an effective record in the directions indicated is fast becoming the exception rather than the rule.

The auditor should have produced to him the stock sheets or inventory of consumable stores adequately certified, and where there are stores ledgers in use he may compare the aggregate balances of the ledger therewith, noting the necessary adjustments. He may check generally the arithmetic of the inventory or actual survey of stock, and satisfy himself that the valuation has been carried out at cost. As to the sales in deliveries from the manufactured stock, the cost records will be available for confirmation of cost. The warehouseman or storekeeper will also have a subsidiary set of books which will furnish a complete record of goods received at the manufactory, the supplies therefrom, and the returns or rejections, which will go far to confirm the quantities as per the general accounts, these books being designed on lines similar to those described in the treatment of general stores.

The auditor, as in the case of the consumable

stores, should examine the stock sheets presented to him which should naturally be properly certified in all essential particulars, and compare the warehousemen's stock balances therewith, noting any necessary reconciliation. He may check the arithmetic of the records of stock actually taken and assure himself in any way that they are correct.

When examining the detailed trading accounts he should note that the principle of valuing the stock of consumable stores and saleable manufactured stock both at the commencement and at the end of the financial period is the same.

The cost accounts will confirm the cost of manufactures in course of completion at the date of the balance sheet.

With regard to amounts received on account of specific contracts in course of completion, or debited to the parties concerned, they will appear in reduction of the item at date, which will be increased by any profit assumed in the accounts on account thereof.

The following points which often occur in the accounts of different kinds of trading concerns may be noted.

A company operating abroad sends timber on consignment to its agents, say, in India. At the end of the financial year, the stock of timber in the possession of the agents is sold, but the account sales has not been sent. In this case the item would appear at selling price less provision for freight and other charges. Stocks in transit would be shown at cost.

In produce companies, any produce of the season, not sold until the ensuing year but before the publication of the annual accounts, is shown generally at realised prices. That unsold would appear at cost.

In dealing with the accounts of Indian trading and other houses, great care must be taken to distinguish between account sale transactions and goods actually bought, and to note the treatment of any advances thereon by the local bank.

It is a prudent course to take the detailed trading account for several years for comparison, noting the relation of gross profit to sales, and the variations in the elements of this synthetic account, making due inquiry into any sums in quantities which have the semblance of being exceptional.

Sometimes it is stated on the face of the balance sheet and in the auditor's report that the stocks have been taken and valued by the management, and though it is often necessary to add words to that effect, the auditor should endeavour to test the correctness of the stock exhibits in the balance sheet. (See also ACCOUNTS, CRITICISM OF, p. 14.)

STOCKHOLDERS, REGISTER OF.

(See AUDITING, p. 71.)

STOCKS AND SHARES.

(See INVESTMENTS, VERIFICATION OF.)

STOCKS IN TRANSIT.

(See GOODS IN TRANSIT, TRADING ACCOUNT, p. 916.)

STOPPAGE IN TRANSITU.

The meaning of this phrase is "stoppage on the way." It is the right of stopping and retaking possession of the goods which an unpaid seller possesses when he receives a notification of the insolvency of the purchaser during the time that the goods are *en route* to the destination named by such purchaser. The notice is generally given to the carrier who will, in the ordinary course of things, have the goods in his possession. To a certain extent it corresponds to the right of lien (*q.v.*), and arises by implication of law. Such implication, however, may be rebutted, for, by the Sale of Goods Act, 1893, where any right arises under a contract of sale by implication of law, it may be negated or varied by express agreement or by the course of dealing between the parties, or by usage, if the usage is such as to bind both parties to the contract.

The right of stoppage on the part of the seller is lost if a bill of lading or other similar document of title has been sent by the vendor to the purchaser, and such bill or document has been endorsed to some third party for value.

Difficulties have frequently arisen as to the time during which the goods are actually in transit. It seems, however, that this must be held to be a question of fact entirely dependent upon the special circumstances of the case.

STORES.

The treatment of stores, so far as the financial books of account are concerned, is a comparatively simple matter. Accounts for each class of stores, according to the information desired, will be opened and debited with the purchases, whilst the opening and closing stocks on hand will be debited and credited respectively, in order that the actual consumption may be ascertained and properly charged. It is, however, very advisable that a statistical record of stores should be kept, quite apart from the financial records, particularly where Cost Accounts are kept. A separate Stores Ledger providing columns for quantities (and, if desired, for values also) is used for this purpose. Accounts are opened for each class of stores, which are debited with the quantities purchased by direct postings from the invoices. The stores when received should be placed in charge of the storekeeper, who, in a Stores Received Book, records the quantities received. This book may be used as the posting medium to the Stores Ledger as an alternative to posting from the invoices. The storekeeper should only issue stores

upon the receipt of a properly authorised requisition note. From the requisition note the stores issued will be credited to the appropriate account in the Stores Ledger. The balances on the Stores Ledger Accounts will at stocktaking times form a check on the stock of stores on hand. Leakages will probably occur, and the Ledger should be adjusted to the actual stock on hand after the differences have been satisfactorily explained.

The auditor should satisfy himself that a proper system of recording the receipt and issue of stores by the storekeeper is in existence. From his point of view, it is preferable that the Stores Ledger should not be kept by the storekeeper, but by some other clerk, by which means a more effective check is exercised upon the stores. He should test the balances of stock on hand shown by the Stores Ledger with the stock shown by the stock lists, and any large differences should be accounted for.

STORES ACCOUNT.

(See COST ACCOUNTS, p. 349.)

STORES AND STOCK RECORDS AND ACCOUNTS.

The stock of one producer is frequently the stores, viz., the raw material or manufacturing requisites of another, as, for instance, wool, cloth, or coal. Distributing houses and retail shops deal only with finished stocks, though necessarily carrying a negligible supply, comparatively speaking, of stores for their own consumption. The principal "stores," so called, are, as a matter of fact, dealers only in finished stocks, part of which are of the nature of household stores. As a consequence the expressions "stores" and "stock" are frequently interchanged or confused, the one being used in the place of the other. For example, phrases in common use are "stock in stores," and "stock of stores," "stores" in the one case denoting a warehouse, or stock-room in the other, raw material and such like. For accountancy purposes, and as regards productive concerns, stores may be defined as comprising raw materials, loose or component parts, fuel and other and less important requisites for any given manufacture, whereas stock denotes the finished product ready for sale. From the nature of the case it follows that the routine work in connection with stocks and stores is in many respects the same. The object to be aimed at, in each case, is to see that the receipt and issues of stores and stock is duly recorded, so that supplies are kept at a certain convenient level, not rising above a certain maximum or falling below a certain minimum; to prevent leakage through negligence or pilfering; also to supply information for cost-keeping and for the correct analysis of the corresponding accounts in the financial books. In the

case of distributing houses and retail shops the problem is simpler than in the case of producers, and the system in common use is sufficiently described in the article on DEPARTMENTAL STORES. In order to avoid repetition, this article is therefore confined to productive undertakings. The following is a description of the general routine in a large and typical manufacture. The system described may be adapted to any class of business and to the handling of either stores or stock, and may be amplified or restricted according to circumstances.

STORES AND THE STOREKEEPER.—The stores are under the immediate control of the storekeeper, subject to the directions of the works manager (or, in his absence, the sub-works manager), to whom,—with the exceptions mentioned below—the storekeeper is responsible for the whole of his work, which includes requisitioning, receiving, inspecting, storing and issue of all material, the maintenance of minimum stocks of each class of material, the keeping of the stores records, and the making of returns to the managing director, the works secretary and the buying department.

The system of storing and recording aims at—

- (1) The safe and convenient arrangement of each class of material.
- (2) The proper accounting for all material received, and used.
- (3) The showing at a glance the stocks on hand and those which require to be replenished.
- (4) The protection of perishable material from damp and dust, etc.

GENERAL DESCRIPTION OF SYSTEM.—The methods pursued are as follows—

(1) **Buying of Material.** The works manager (or in his absence the sub-works manager), is responsible for all the buying (except of stationery, printed and advertising matter, including blocks and electros, packing cases and materials for which the works secretary is responsible).

(2) The works managers and works secretary are ultimately responsible to the managing director for there being at all times adequate stocks kept in store of the materials for which they are respectively responsible.

Storing of Material. Bulky materials are stored in separate sections of the warehouse duly partitioned off and numbered in sequence.

Material small in bulk (such as screws and small parts), or of a perishable nature (such as stationery and printed matter), are kept in bins, also numbered in sequence.

Each class or type of material is given a distinguishing symbol. The buying department is responsible for the immediate allocation of symbols to any new material which is ordered and taken into stock, and the storekeeper for the provision of a section or bin for the storing of same, taking his

instructions as to details from the works manager.

There is attached to each separate section or bin—

(1) A ticket (Form A) bearing the name and distinguishing symbol of the contents.

(2) A sectional card (Form B) on which are entered—

(a) The maximum and minimum stock to be carried of the material in the section or bin.

(b) The quantities of each and every delivery of goods into, or issued out of, the section or bin.

Form A.

SYMBOL

	—					
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DESCRIPTION

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NOTE.—The balance between stock, plus deliveries, less issues, is carried out daily on the sectional card, so as to show from day to day the actual amount of stock, as compared with the minimum, and assist the requisitioning of further supplies in good time.

Where more than one section or bin is in use for the same class of material, tickets are attached to the additional receptacles, on which are entered the number of the original section or bin, together with, and in proper sequence, distinguishing letters in alphabetical order, thus: I.A., I.B.

A subsidiary sectional card, with the number and letter of each additional receptacle, is attached to the receptacle *first in use*, so that the total stock may still be readily compared with the minimum.

The sectional cards, taken as a whole, are equivalent to a Stores Ledger, with the advantage that each balance can be readily, and, if necessary,

Form B.

FOR WEIGHTS

SYMBOL

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DESCRIPTION

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STOCK

	T.	C.	Q.	L.
MAXIMUM.				
MINIMUM				

RECEIVED.

ISSUED

RECEIVED.					ISSUED													
DATE.	WEIGHT.				DATE.	WEIGHT.				CARD NO.	BALANCE.	DATE.	WEIGHT.				CARD NO.	BALANCE.
	T.	C.	Q.	L.		T.	C.	Q.	L.				T.	C.	Q.	L.		

Form B.

FOR QUANTITIES

SYMBOL

	—					
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DESCRIPTION

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STOCK

MAXIMUM
MINIMUM

RECEIVED.

ISSUED.

RECEIVED.					ISSUED.				
DATE.	QUANTITY.				DATE.	QUANTITY.			

simultaneously tested and agreed with the stock, not only at stocktaking, but at any time. From these cards the storekeeper makes a return, at stated intervals, of stocks on hand to the managing director and works manager. The details on the cards are from time to time compared with the Bought and Sold Day Books by different members of the staff, thus ensuring an independent check upon the correctness of the entries.

The routine work necessary to operate the system is fully described in the following standing orders, which the storekeeper has to observe and enforce—

STANDING ORDERS TO STOREKEEPER.

(1) **Issuing from Stores.** On arriving in the morning, first issue all material required for use in the factory during the day.

(2) Issue same only against a numbered requisition slip (Form C) received from and signed by the works foreman. (See below).

(3) Record on the sectional cards quantities issued to works, or, in case of stationery, to the office. Carry out the balance remaining in stock so that each card shows at a glance the stock on hand (material put into stock being recorded on the sectional cards in the same way).

(4) After careful checking, these slips should be sent to the counting-house, to be dealt with by the stores ledger clerk.

(1) **Receipt into Stores.** Check and book in subject to inspection the quantities or weights of all goods delivered to the company.

(2) See that same are in accordance with the advice notes by which they should be accompanied. (See Order Form D, p. 899.)

(3) On receipt of any goods enter daily, *without fail*, in the Goods Inwards Book the following particulars—

1. Date of delivery.
2. The company's order number.
3. The sender's name.
4. A short description of the goods.
5. The quantity or weight actually delivered.

6. Name of carrier or railway, and whether delivered carriage forward or paid.

7. Remarks (if any).

8. Quantity approved and put into stock.

This book must be written up every day. Should any discrepancy be found in the advice notes the note in question is to be at once sent to the buying department, with particulars of the discrepancy, a note being also made in the Goods Inwards Book in the column for remarks.

(4) Compare particulars as entered in the Goods Inwards Book with the copies of the orders in the Company's Order Book (see Form D, p. 899) received from the buying department, and if correct, tick off col. 2 of the Goods Inwards Book.

In addition to the advice notes, the Goods Inwards Book is available to the Bought Ledger department, for the purpose of checking invoices inwards as regards weights or quantities. It is convenient, therefore, to have two books, one for Monday, Wednesday, Friday; the other for Tuesday, Thursday, Saturday.

(5) See personally (or, if that be impossible, by qualified understudy) that the goods received are correct as to quality and description, carefully observing rules as to inspection of material, as below, and entering the result of inspection in "Remarks" column of Goods Inwards Book.

Inspection of Material. The rules are as follows—

(1) In case of doubt as to any *ordinary* material, at once submit it, or a representative sample of same, to the works manager for acceptance or rejection, and await his report.

(2) After inspecting such materials as stationery or printed matter of any kind (whether labels, boxes, advertising material, showcards or stationery pure and simple) report to the advertising department as to the manner in which they were packed and delivered. If, on taking out 2 per cent. from the various packages, the articles are found to be damaged owing to bad packing,

Form C.

Date.....

No. 28100.....

RAW MATERIAL Issued from Stores to.....Dept. for Job No.....

Quantity.	Weight.		lbs.	Description.	Symbol No.	Charge to.
	cwt.	qrs.				

Issued by.....

Received by.....

Foreman.

Form D.

A B COMPANY, LTD.

TELEGRAMS :
"LONDON."

Order No.

TELEPHONE :

Date

19

To

Please Supply

DELIVERY

PACKING

CARRIAGE

For A B COMPANY, Limited.

TERMS.—Best Trade Terms, and 2½ per cent. for Cash on or about 25th day of month following delivery. If the above order is not clear in all details, please advise before putting in hand.
No variation in the terms of this order will be accepted unless notified within Three Days of Receipt.
Advice Note and Priced Invoice, stating Order No., must be posted same day as goods are dispatched. Accounts will only be passed for payment on receipt of Monthly Statement.

IMPORTANT.—In the event of any query, please ring up Buying Department.

advise buying department at once and await the instructions of that department before putting the material into stock.

(3) Submit a sample of each of the articles mentioned in the foregoing paragraph to the works secretary.

(The works secretary *initials* same as correct, and, where the printing is in a foreign language, instructs the storekeeper exactly what it is and for what purpose.)

(4) See also that one sample (except of showcards and cardboard boxes) is neatly pasted in the Loose Leaf Guard Book which is kept in the buying department.

(In the case of showcards, see that a sample of every one is sent up to the buying department to be framed and put with the others; and in the case of boxes, see that a sample (neatly labelled with order number, name of manufacturer, date of the first delivery, and a short description of the box) is sent up to the buying department to be filed away.)

(1) **Special Inspection.** *In any case* send out

the material of which the following is a list to the inspecting department to be passed—

(Here should be entered a list in detail according to circumstances.)

(2) In the case of large deliveries of any of the special goods which have to pass through the inspection department, if for any reason they cannot be inspected at once on arrival, personally pick out at random 2 per cent. of the quantity delivered and hand over same to the *works foreman*, accompanied by Form E, *which has to be made out by the storekeeper for all goods handed to the inspection department*. The works foreman must see that this 2 per cent. is inspected immediately by the inspection department, which will report on the yellow form (E) in the space provided

(3) On receipt of the inspector's report on the 2 per cent. and the goods (which happen concurrently), and as soon as satisfied that the material as delivered is correct and passed, post the quantity delivered and passed into stores into the Goods Inwards Book, and post same to the sectional cards. Also endorse same on the back

A. B. COMPANY, LTD.**DELIVERY AND INSPECTION REPORT**

By whom to be filled up	Date of present Delivery 19....	
STORES ON ARRIVAL.	Goods received from :—	
	Nature of Goods :—	
	No of present Delivery :—	Date of previous Delivery :—
	Quantity of present Delivery :—	Total delivered to Date :—
STORES FROM INSPECTION DEPT.'S REPORT OR AS RESULT OF COUNTING OR VISUAL INSPECTION.	Quantity checked by :—	
	Date handed Inspection Dept. :—	
	Quantity accepted :—	Total accepted to Date :—
	,, rejected :—	,, rejected ,, :—
	Reasons for rejection :—	
	Nature of inspection or check :—	
BUYING DEPT.	Date when accepted portion returned to Stores from Inspection Dept. :—	
	Received by	(Storekeeper).
	Price and Terms :—	
	Allocate to :—	
	Date when Manufacturers advised of rejections :—	
ACCOUNTANT'S DEPT.	,, ,, rejected goods returned to Manufacturers :—	
	Advice sent by :—	
	Quantities, etc., noted on Invoice by :—	
	Debit Note for rejections sent by and date sent :—	

of the stores copy of the order (received from the buying department).

(4) As soon as the deliveries mentioned on the order have been completed (including the replacement of any rejections which have been returned to the manufacturers) return stores copy of order duly endorsed as mentioned above to the buying department.

(5) If the result of the inspection of the 2 per cent. points to the whole consignment being returned, always take final instructions as to this from the works manager or buying department. Lay before them the inspector's written report on the sample, and get him to endorse the report with a note as to whether the goods are to be accepted subject to subsequent inspection of the whole quantity, or whether the whole consignment is to be returned to the manufacturer.

Make entries accordingly.

(Complete inspection must in all cases be carried out with as little delay as possible, and the storekeeper must put before the works manager every week a list of all articles waiting for inspection with the date when they were delivered, and send a copy of this list to the head of the inspection department.)

(6) Enter the result of the inspection as finally settled by the works manager, in the Goods Inwards Book.

Reports to Buying Department. (1) Advise the buying clerk whether or not goods ordered have been delivered by due date. For this purpose

keep a diary, and on receipt of the copies of the orders from the buying department, make a note under the date, or dates, on which deliveries of anything ordered are due, so as to show at a glance each day what ought to come in, and exactly what has or has not been delivered. Cross out all lines as delivered, so that the buying clerk can see at a glance what has and has not been delivered, and how long orders in arrears are overdue.

Requisitioning Supplies. (1) Record the minimum stocks to be maintained of all lines on the space provided for the purpose at the top of the sectional card.

(2) In the case of any new article, ascertain from the works manager what the minimum should be and at once enter same on the Sectional card.

(3) Requisition the buying department for supplies before the stocks, as shown by the "Balance" column on the sectional card, have fallen below the minimum.

NOTE.—*The storekeeper is to assume that every article is a stock article and TO BE REPEATED, until he receives instructions in writing from works manager that any line has become obsolete.*

(2) Keep separate books for requisitions (Form F) for (a) all goods consumed in the factory, (b) stationery.

Requisitions coming under (a) are to be countersigned by the works manager, and taken direct by the storekeeper to the buying clerk. If any

Form F.

TO BUYING DEPARTMENT.

Department

19...

Please order goods as under :—

QUANTITY.	DESCRIPTION.	STOCK.	SUPPLIER.	PRICE.	REQUIRED FOR.

Delivery required ex Contract :—

Please urge delivery of :—

Signature _____

printing be involved, the requisition must also be countersigned by the works secretary.

Requisitions coming under (b) are to be taken to and countersigned by the works secretary.

Periodical Returns as to Stores on Hand. Prepare at such regular intervals as may be from time to time laid down by the managing director a statement of the balances on all the sectional cards.

NOTE. This return, of which each separate sheet is in pad or block form, is made out in duplicate with a carbon, each sheet being signed by the storekeeper. One complete set of the sheets is sent up to the works secretary to place before the managing director, and the other complete set to the works manager, within three working days of the date up to which the return is directed to be made.

Alterations in the Routine. No variation in the existing routine, forms, cards, etc., is to be introduced without the sanction of the works manager or the works secretary, whichever is responsible for the particular branch of the stores in which alterations may be contemplated or considered advisable; but the storekeeper is at liberty at any time to put before either of them, as the case may be, for reference to the managing director, any suggested improvements that he may consider advisable.

The foregoing particulars show how the various store records are kept, and that they admit of continuous checking and control. The book-keeping department obtains the information it requires for the financial books from the various forms or counterfoils of same duly verified and signed, and from the Goods Inwards Book or the delivery notes by which the invoices are checked and dissected (see INTERNAL CHECKS), and is able to sub-divide the purchases accordingly by means of a columnar Day Book. The quantities of stores may be verified by reference to the sectional cards, or to the Stores Ledger, if such be kept in addition to the cards, of which it would be a replica, but of a fixed nature. (The question of costing is dealt with in a separate article.)

STOCK AND THE WAREHOUSEMAN.—As already mentioned, much of the routine work is the same as in the case of stores, especially as regards buying, storing, and recording quantities, and need not be repeated. The principal difference is that whereas stores are bought from outside suppliers, stock may be solely the finished product of the factory, or it may be bought from other sources, or partly the one and partly the other. In the one case the warehouseman receives with the goods a works ticket (see INTERNAL CHECKS), in the other the supplier's delivery note, just as in the case of stores. These particulars are entered in the Stock Day Book, which is a connecting link between the works and the warehouse

Form G.		Folio 1.	
ARTICLE		MINIMUM STOCK	
DATE RECEIVED.	FROM	QUANTITIES.	WEIGHT. T. C. GR. LB.
PRICE.	S.D.B. FOLIO.	INVOICE VALUE. £ s. d.	DATE ISSUED.
CHARGE TO	QUANTITY.	WEIGHT. T. C. GR. LB.	PRICE.
S.D.B. FOLIO.	VALUE. £ s. d.	Folio 1.	MINIMUM STOCK

on the one hand and the warehouse and the counting-house on the other. Full details should be entered in the Stock Day Book, including the numbers of the works tickets or the delivery or advice notes. Two Stock Day Books are kept for use on alternate days. The counting-house checks the Stock Day Book by reference to the duplicates of the works tickets and advice notes and the invoices received from the supplier, as explained in the article on INTERNAL CHECKS. The issue of stocks is made as described in the article on INTERNAL CHECKS, and the Stock Day Book is written up from the duplicates of advice notes referred to in the same article. From the Stock Day Book the warehouseman writes up the Stock Ledger, entering receipts on the one side and issues on the other. The Stock Ledger may be in the form shown on page 902, or an adaptation of same.

The Stock Day Book is similar in form but without the headings "Article," "Symbol No." or "Minimum Stock," which form separate columns inserted next to date received on the one side and date issued on the other.

SUBDIVISION OF LEDGER.

(See LEDGER.)

SUBPOENA.

This is the name given to the document which is issued, on the application of any of the parties to the proceedings, by any Court of Justice demanding the attendance of a specified person, that is, the person to whom the document is addressed, to give evidence in a particular cause or matter. The term is derived from two Latin words *sub poenâ*, "under a penalty," and is so called because it names a penalty to which the person summoned is liable in case of disobedience. There are two kinds of subpoena, one, the *subpoena ad testificandum*, for the purpose of procuring the attendance of a witness simply to give evidence, and the other, the *subpoena duces tecum* for the purpose of compelling a person to produce certain specified documents for the inspection of the Court. Whenever a subpoena of either kind is served, it is necessary that there should be paid to the person who is required as a witness a sum of money which is sufficient to cover his reasonable expenses in attending Court. This is called "conduct money" (*q.v.*). If this amount is not paid, no liability is incurred by non-attendance at Court or by a refusal to give evidence. But if the witness is actually in Court at the time when the case is called on, even though no conduct money has been paid to him, it would appear that he cannot then decline to give evidence.

A subpoena which is issued for the purpose of summoning witnesses may contain any number of names, if necessary, but a subpoena of the other

kind cannot contain more than three names, and a party suing out the same may require a separate subpoena for each party summoned if it is deemed advisable to adopt this course.

The subpoena must be served within twelve weeks of the date of its issue, and it remains in force, in the case of actions or matters tried in the High Court in London, from the date of its issue until the action or matter has been heard. If the action is one tried with a jury and the jury disagree, it appears that if a re-trial takes place a fresh subpoena must be issued for the second trial. If the subpoena is issued in respect of an action or matter at the Assizes, it is in force only during the period of the Assize for which it is issued. A fresh subpoena must be issued in case either of an adjournment of the trial or of a new trial.

SUBSCRIPTION CASH BOOK, AUDITORS AND.

(See AUDITING, p. 102.)

SUBSCRIPTION, MINIMUM.

(See MINIMUM SUBSCRIPTION.)

SUBSCRIPTIONS AND DONATIONS (Paid).

In recording subscriptions and donations in the books of account, distinction should be made between purely voluntary subscriptions and donations, which are not allowed as deductions for income tax purposes, and subscriptions and levies to certain employers' federations, and to trade protection societies and agencies, which are. Separate accounts should be opened for each class, so that the computation of the assessment to income tax may subsequently be facilitated.

The auditor should direct his attention (1) to verifying the power (in the case of joint stock companies) to subscribe by reference to the Articles of Association, or private Act of Parliament, or Royal Charter, as the case may be; (2) to the Directors' Minute Book, or, in the case of a grant by the company in general meeting, to the Shareholders' Minute Book, for the minute authorising the payment and its amount; and (3) to the production of the receipt vouching the payment. Charitable institutions are exempt from Stamp Duty on receipts.

SUBSIDIARY ACCOUNTS.

(a) Accounts kept to give detail of a principal account to which they have to be closed; for example, in a trading business the Purchases, Sales and Stock Accounts are subsidiary to the Trading Account, and this, together with the remaining Nominal Accounts are subsidiary to the Profit and Loss Accounts; in a manufacturing business the accounts for the various productive costs are subsidiary to the Manufacturing or Production Account.

(b) Accounts kept which do not form part of the accounts, but which run collaterally therewith, as, for example, Cost Accounts, the total of the results shown by which should agree with the total cost of goods produced shown by the Manufacturing Account.

SUBSIDIARY BOOKS.

The books of prime, first, or original entry, and in an ordinary trading business comprise Invoice Book, Day Book, Inwards and Outwards Returns Books, Journal and Cash Book, so called because they are subsidiary to the Ledger, which is the principal book of account, and to which particulars of the transactions are posted.

SUCCESSION DUTY.

(See EXECUTORSHIP ACCOUNTS, p. 461.)

SUI JURIS.

Although not capable of an exact translation, this Latin phrase is easily comprehensible, and when it is applied to a person it signifies that he or she is capable of acting without the intervention of any other person. *Primâ facie*, every person, other than an infant or a lunatic, is *sui juris*. Any person who is subject to the control of another is said to be *alieni juris*.

SUMMARY CASES.

These are cases which are heard and determined in the local Police Courts, and they are so called because, under the provisions of special statutes, it is permissible to try certain classes of them without the elaborate procedure obtaining in the higher courts. A court of summary jurisdiction is presided over in some of the larger towns of the country by a stipendiary magistrate, whose powers correspond to those of the metropolitan magistrates for the various districts of London. If there is no stipendiary magistrate, summary

cases are heard by the local justices, and it is necessary in the majority of cases that two of these should be sitting together.

SUNDRIES LEDGER.

A special Ledger kept for the reception of the accounts of sundry persons having only odd transactions with the firm. A convenient form to adopt is either a Loose-Leaf Ledger or an ordinary Ledger indexed through alphabetically. As these accounts are not looked upon as being established accounts, they are kept under constant supervision, and prompt payment is required.

The Ledger may be arranged so as to serve the dual purpose of Day Book and Ledger, when full detail will be entered, and in all cases where it is desired to see at a glance the full particulars of goods supplied to each customer, this is advisable. In this case the detail will not appear in the Day Book, which then takes the form of a summary of totals in order to arrive at the total sales.

SUNDRY CREDITORS.

(See AUDITING, p. 88.)

SUNDRY DEBTORS.

(See AUDITING, p. 94; BALANCE SHEET, p. 151.)

SUNDRY PERSONS ACCOUNT.

An account kept in both Debit and Credit Ledgers for persons with whom only odd transactions are had. Instead of the entry being made "To Goods," or "By Goods," the name of the debtor or creditor is inserted with full address, as these items are not indexed in the customary manner. A wise course to adopt when most of the accounts on any page are paid, is to carry forward the remainder so they are not overlooked, and a strict eye should be kept on any small balances left owing.

The following is an example of a Sundry Persons Account—

Dr.		SUNDRY PERSONS ACCOUNT						Cr.	
19..		D.B. Folio.	£ s. d.			19..		C.B. Folio.	£ s. d.
July 1	To A. Smith, 13 Market Street, Oldham . .	1	2	9	6	July 4	By A. Smith, Oldham . .	97	2 9 6
" 3	" T. Nelson, Duke Street, Chadderton . . .	3	1	7	9	" 10	" T. Nelson, Chadderton . .	101	1 7 9
" 7	" D. Jones, Draper, Llanfair	7		5	7				
" 11	" T. Kelly, 3 Anne Street, Darwen	10	3	9	6	Aug. 8	" T. Kelly, Darwen . . .	169	2 0 0
" 14	" Bon Marché, Sale, Cheshire	19		7	3	July 16	" Bon Marché, Sale, Cheshire	110	7 3
" 15	" E. Gardner, High Street, Tunbridge Wells . .	21	1	3	6				

SUPERANNUATION FUND.

Contributions to the fund made by the business form a charge against the profits. Compulsory contributions by the employees will be deducted from the wages payable and credited to the fund. Interest on the fund must be periodically credited, whilst payments to superannuated employees and the necessary expenses of administration will, subject, in the case of the latter, to the company having so determined, be debited to the fund.

It will be the duty of the auditor to see that the proper contributions are received from employees, and that a correctly proportionate contribution by the business is charged against profit. He will verify the payments both to annuitants and for expenses by requiring the production of proper receipts. Where the company undertakes the actuarial soundness of the fund, a periodical valuation must be made and any deficiency must be adequately provided for. If the fund is represented by specific investments, the auditor must examine the scrip, certificates of registration, bonds, etc., in order to verify the existence of the investments, and must see that all interest due is received and all accruing interest brought into account. (See PENSION FUND ACCOUNT, ANNUITIES TO EMPLOYEES.)

SUPER-TAX.

(See INCOME TAX APPENDIX, p. 945.)

SUPRÀ PROTEST.

(See BILL OF EXCHANGE, PAYMENT FOR HONOUR.)

SURETY.

(See GUARANTEE.)

SURPLUS ASSETS.

Assets not required for the purposes of a business in its existing state.

SURPLUS OF PROFIT.

(See BALANCE SHEET, p. 143.)

SURRENDER OF SHARES.

A surrender of shares in a limited liability company can only be accepted in a case where a forfeiture would be justified. Commonly, the articles of a company authorise the directors to accept such a surrender, which, of course, makes it necessary for them to undergo the usual formalities in connection with the procedure of forfeiture when the shareholder is willing to surrender his interest.

It must be remembered that if a surrender can be interpreted as a purchase by the company of its shares, or that the transaction has been carried out, or is proposed to relieve a member from his liability, it is void. There are, however, one or two particular phases of the subject, which are now and then exemplified in the accounts of public companies.

For example, the A Company is formed for the purpose of carrying out the objects of its memorandum, and in particular for the purpose of acquiring and working certain properties. One of the properties is acquired from X in satisfaction of which £5,000 is paid in cash, £7,500 by way of allotment of shares as fully paid, and £2,500 in debentures. Partial failure of expectations causes the vendor to surrender his shares and debentures, which fact may be recorded in the balance sheet as under—

	£	£
Purchase of Properties	15,000	
Less Surrender of Shares and Debentures as below	10,000	
	<hr/>	5,000
(Here would be stated brief details of the shares and Debentures)		10,000

The shares must, of course, remain as issued; usually they are put in the name of some one on behalf of the company. The debentures surrendered may be credited to the Debenture Account instead of being treated as shown, according to the circumstances.

In a particular case in practice fraud was discovered after the purchase had been completed and satisfied, and the vendor conveniently disappeared. The shares which had been allotted in part payment were treated in a manner similar to the foregoing.

SUSPENSE ACCOUNT.

An account raised for the reception of items which cannot for any reason be allocated to their correct account, or items held over until disputes, etc., in connection with them are settled, e.g. in the case of an action pending at the date of balancing, this affects the accounts for the period for which the books are being made up. An amount sufficient to cover the claim is, therefore, credited to "Suspense Account" and charged against the period. When the result is known, the Suspense Account is closed according to the facts, being either credited back to profit or otherwise dealt with.

At the period of making up the accounts of a firm when adjustments require to be made for expenses due and accruing, and for payments made in advance, such items are sometimes

placed to a "Suspense Account," but this method is not technically correct, as they are not in suspense but are actual adjustments, the better method of treatment being to bring them down to the contra of the account to which they belong in the new period.

SUSPENSION OF PAYMENT.

The stoppage of payment of debts due to other persons.

SYNDIC.

This term may be used to apply to any body of persons invested with a particular legal status. But it is most frequently applied in connection with foreign bankruptcies, and then it generally means the person who corresponds to the trustee in bankruptcy in English law.

SYSTEMS OF ACCOUNT.

(See AUDITING, p. 85.)

TABULAR LEDGER.

THE title given to a special Ledger which has come into general use for hotels and other businesses, in which the majority of the customers' accounts are only of short duration and made up of small items, the Personal and Nominal Ledger entries being combined in tabular form. The system is carried out by means of an analysis, the object being to reduce and expedite the work of dealing with masses of detail, and to keep the accounts so up to date that the bills may be rendered at a moment's notice.

In hotels the Day Book is entered under each name, with full particulars of everything supplied each day; the items are analysed at the foot of each entry and posted to the Visitors' Ledger (p. 908), the left-hand columns in which are headed with the numbers of rooms and names of visitors, and give the particulars required for making up the bill, which is usually kept made out up to and including the preceding day.

The amount owing by each visitor is brought forward from day to day, so that his total indebtedness is readily ascertainable, provision being made at the foot of each page for amounts paid, allowances, and balances carried forward to the next day.

The right-hand columns are used for the reception of the total amounts under each Nominal heading supplied to visitors for the day, those brought forward from the previous page and the total carried forward, thus giving the Nominal Accounts.

Tabular Ledgers may be used advantageously for all businesses where only short credit is given, as tailors, dressmakers, newsagents, etc., and for gas, electricity, water, telephone subscriptions, and rent accounts.

TAILOR. DAY BOOK—LEDGER

Order No.	January.			Ledger or C.B. Folio.			
1184	T. R. Jack— Suit	3	10	0	C.B. 100	3	10 0
1185	R. S. Wilkins— 2 Pairs Trousers	1	10	0			
1186	W. Robinson— Overcoat 1 Pair Trousers 1 Vest	2	10	0			
1187	H. Thomas— Dress Suit	4	4	0	C.B. 105	4	4 0
1188	T. Roland— Frock Coat & Vest	4	4	0	C.B. 108	4	4 0
1189	G. Black— Suit Trousers Etc. Total for period to Sales A/c	3	16	0			

GAS RATE LEDGER

Progressive No.	No. of House.	NAME.	Amount due on Jan., 19.., brought forward.	Meter Index.		Consumption (Thous. sands.)	Gas at 3/4 per 1,000.		Meter Rents.	Date Received.	C.B. Fol.	Amount Received.	Allowance Book.		Quarter ending June 30, 19..	Quarter ending Sept. 30, 19..	Quarter ending Dec. 31, 19..	Amount due on Dec. 31, 19.., carried forward.	Remarks.
				From.	To.		£	s. d.					A/c.	Fo.					
1762	1	Western St.	£ 216 8	17620	17780	16.0	£ 213 4	2 6	£ s. d.	19..	56	£ 216 8	£ s. d.						
1763	2	Jones, A.	210 0	06915	07060	14.5	218 4	2 6	216 0	Feb. 15	64	210 0	216 0						
1764	3	Brown, B.	113 4	27010	27118	10.8	116 0	2 6	113 4	" 22	73	113 4	113 4						
1765	4	Robinson, C.	4 3	41562	41782	22.0	313 4	5 0	4 0 0	Mar. 1	42	4 0 0	4 0 0						
1766	5	Smith, D.	£11 3 4	93107	93740	63.3	£10 11 0	12 6	£11 0 0	Feb. 1		£11 0 0	3 4	Allee. 71					

VISITORS' LEDGER

HOTEL

DEBITS.	Mr. Roberts.		Mr. Burns.		Mrs. Wilson.		4.		5.		DEBITS.		Daily Total.		Bt. Forward.		Cd. Forward.				
	£	s.	£	s.	£	s.	£	s.	£	s.	£	s.	£	s.	£	s.	£	s.			
Balance brought forward													3	14	0						
Apartments			1	2	0	6							11	0	2	3	0	2			
Attendance		2		5		0							7	6		12	0	14			
Baths				2		6										2	6	19			
Fire and Lights																		6			
Boarders																					
Breakfasts																					
Luncheons																					
Dinners		2		2		6							4	6		12	6	17			
Dessert and Ices		6		7		0							5	0		9	6	14			
Sandwiches													13	6		19	0	12			
Tea and Coffee																					
Soups																					
Suppers																					
Servants' Board																					
																16	0	16			
Wine		4		3		6							10	0		6	0	16			
Spirits																					
																1	0	1			
Ales, Stout, etc.																					
Minerals							1	6						1	6		6	2			
Cigars		2		0		6								2	0		6	0			
Stationery																					
Newspapers																					
Postage																					
Paid Out																					
Washing																					
Carriage																					
Billiards																					
Total		17	6	1	16	0	3	15	6			Total	6	9	0	6	6	9	1	6	
CREDITS.																					
Overcharges																					
Cash Received																					
Ledger Account																					
Balance carried forward		17	6	1	16	0	3	15	6			Overcharges									
												Cash Received	1	16	0	2	12	6	4	8	6
Total		17	6	1	16	0	3	15	6			Ledger Account									
												Balance carried forward	4	13	0				4	13	0
												Total	6	9	0				9	1	6
Folio Ledger Account												Folio Ledger Account									
Transferred to												Transferred to									

TABULATING MACHINES.

(See OFFICE MACHINES AND APPLIANCES.)

TAX, INCOME.

(See APPENDIX, p. 945.)

TAXATION OF COSTS.

When no special bargain has been made between a solicitor and his client with respect to the costs to be charged in any particular matter, the costs must not be fixed at an exorbitant rate. If, then, the bill of the solicitor when it is delivered to his client is considered too high, the matter may be taken before an official who is known as the Taxing Master, and this official decides which items are fair and proper, and which ought to be reduced. A similar kind of procedure is in vogue when the successful party in litigation is awarded costs, and the opposing party refuses to pay on the ground that they are exaggerated. The Taxing Master again decides what is the reasonable amount to be charged, and eventually gives his *allocatur* (*q.v.*) for that amount. The costs incurred through this process of taxation must be paid by the person who demands the taxation, unless the bill is reduced by at least one-sixth of its total amount. (See also LIQUIDATORS, ACCOUNTS OF, p. 687.)

TAXES.

(See PROFIT AND LOSS ACCOUNTS, p. 791; RATES AND TAXES.)

TENANCY FROM YEAR TO YEAR.

A tenancy of this nature arises when lands or buildings are let by the landlord to the tenant from year to year by express contract, or even when there is no express contract if the rent reserved is calculated by the year, or even when a tenant holds over after the expiration of his term and pays rent in respect thereof. The Courts have always leaned, whenever possible, to construing a tenancy as being one of this character, even though the rent may be payable by half-yearly or quarterly instalments. If, however, there are any concomitant circumstances which might lead to a contrary conclusion, the payment of the rent will generally be a decisive factor, and in the cases just instanced, the tenancy would be either a half-yearly or a quarterly one. Naturally in any cases where the rent is paid monthly or weekly it would be somewhat difficult to construe the tenancy as being other than a monthly or a weekly one.

By the Statute of Frauds, tenancies for a period not exceeding three years and where the rent reserved is at least two-thirds of the improved value of the premises may be made by word of mouth. Tenancies for a period exceeding three years must be by deed, but if a tenancy purports

to be created for a longer term than three years, and the tenant actually enters into possession, although he is in under a lease which is void as not complying with the statute and, therefore, is liable to be ejected, nevertheless, if he pays any rent in respect of his holding, he becomes a tenant from year to year, and all the incidents of a yearly tenancy apply. As to the right of a tenant to enter, where there is neither a written agreement nor a deed in existence, see LEASES.

A letting for "one year certain, and so on from year to year," is a tenancy for two years at least, unless there is some special stipulation between the parties as to the termination of the tenancy at the end of the first year.

The mutual obligations of the landlord and tenant as to the demised land or premises are generally arranged at the time of the agreement being made between the parties. In the absence of any such special arrangement, the landlord is not bound to do anything with respect to the premises, and the principal duty imposed upon the tenant is to keep the premises, if it is premises that are let, wind and water tight.

A yearly tenancy is terminated by a half-year's notice on either side, but the notice must expire at the end of the current year of the tenancy.

TENANCY IN COMMON.

When land is held by several individuals and not by one person only, and each of them has a separate and distinct share in the land which can be conveyed or disposed of by will, or inherited by the representative of any of those who die, this is called "tenancy in common," as distinguished from "joint tenancy" (*q.v.*). Whenever land is devised to several persons and these persons are not designated as tenants in common, a joint tenancy is always presumed; but if a tenancy in common is expressly created, it is possible for the creator of the same to give either equal or unequal shares to the beneficiaries. There are very obvious inconveniences attached to a holding of this character, and the general course to be adopted is for the tenants in common to divide up the estate into proper proportions by means of a partition suit in the Chancery Division of the High Court, which division has express jurisdiction in such matters under the Judicature Act, 1873.

TENANT AT WILL.

This is a person who holds under a tenancy which is determinable at any time by either the landlord or the tenant. Though it may be created expressly, it more generally arises when a tenancy has been created contrary to the provision of the Statute of Frauds, as, for example, where a landlord leases land to a tenant for a period of more than three years, or at a rent which is less than

two-thirds of the rack-rent by parol. But if the tenant enters into possession and pays rent, the tenancy at will is changed into a tenancy from year to year, and all the incidents of such a tenancy attach at once. It is only necessary to add that a tenant at will is always entitled to emblements (*q.v.*) when the tenancy is determined by the act of the landlord.

TENDER.

This word has more than one meaning in law. In the first place it signifies the offer which is the preliminary step in the formation of every contract. Secondly, it is an attempt to perform the terms of a contract. Thirdly, and this is the most common use of the term, it has reference to the offer of a sum of money in settlement of an account so as to terminate an outstanding obligation. When a tender is made, its validity depends upon its fulfilling the following conditions—

(a) The full amount must be actually produced unless the creditor expressly dispenses with or prevents its production. It must be of the whole debt, and no change can be demanded.

(b) It must be unconditional.

(c) It must be made to the creditor himself, or to an agent duly authorised to receive payment.

(d) It must be in the current currency of the realm.

The fact of tender having been made does not extinguish the debt. But if the money is refused, the debtor should, upon action being brought, pay the sum into Court with a plea of tender. If the creditor then obtains only a sum equal to or less than the sum thus paid in, the creditor, although successful in his action, will have to pay the costs incurred since the date of the payment in. (See also **LEGAL TENDER.**)

TENENDUM OF A DEED.

That part of a deed, in the conveyance of property, which contains the words "to hold." The general words used in full are "to have and to hold," the words "to have" being technically known as the "*habendum*." As to the use and meaning of the words, see **HABENDUM OF A DEED.**

TENURE.

This term has been defined by an authority, who is always considered in the light of a classic upon matters relating to real property, as the relation between a feudal lord and the tenant of land. More generally it may now be described as the system of holding lands or tenements in subordination to some superior. Naturally, it owes its origin to the feudal system, when the king or one of the greater barons let out his lands on condition that the tenant or tenants should render certain defined services. To the history of the subject no doubt must be ascribed the fact

that to-day even the practical owner, as we should say, of an estate has no higher legal designation than tenant in fee simple, that is, the name "tenant" still remains although the services of former days are matters relating entirely to the past.

TERMINAL COSTS.

(See **COST ACCOUNTS**, p. 348.)

TERMINATING BUILDING SOCIETY.

(See **BUILDING SOCIETIES.**)

TESTAMENTARY EXPENSES.

(See **AUDITING**, p. 121; **EXECUTORSHIP ACCOUNTS**, p. 450.)

TESTATOR'S ESTATE, AUDIT OF.

(See **AUDITING**, p. 67.)

THEATRE PROPRIETORS, AUDITORS AND.

(See **AUDITING**, p. 116.)

THINGS IN ACTION.

(See **CHOSSES IN ACTION.**)

THINGS IN POSSESSION.

(See **CHOSSES IN POSSESSION.**)

THIRD PARTY.

It sometimes happens when an action at law has been commenced that the whole question in dispute cannot be conclusively fought out as between the plaintiff and the defendant, but that some other person or persons is or are involved, especially in a case where the defendant claims to have some remedy over and against some individual or individuals, in respect of the contract or tort for which he is being sued by the plaintiff. Such person or persons is or are called a "third party" or "third parties," and upon taking the proper procedure this third party or these third parties will be brought into the case so that the whole matter in dispute may be disposed of once for all.

TILL TAKINGS.

Where till takings embrace both cash sales and sums received in payment for credit sales, separate entries must be made in respect of each in the Cash Book. The cash sales may be entered in total daily, and posted to the Cash Sales Account, or, preferably, a separate column may be provided for their record in the Cash Book, and the total of the column posted monthly, or at other convenient periods. Credit sales takings must be entered in detail, either in the Cash Book or in a subsidiary Credit Sales Cash Book (the daily total of which is carried to the General Cash Book) and the

personal accounts of the debtors credited by postings therefrom.

All the till takings should be banked in one item, if possible, daily, any cash payments being made through the petty cash, and not out of the takings.

The auditor should require the production of the till-rolls, and compare the totals of the rolls with the entries in the Cash Book. A record of "shorts and overs" should be kept and any serious deficiencies or surpluses enquired into. Where the till-rolls are automatically added by the machine it is unnecessary to check the additions of the rolls; but otherwise they should be thoroughly tested. In cases in which the till registers the total receipts but does not print them on the rolls, they should be regularly examined by a responsible person, whose certificate of the daily amounts registered should be produced to the auditor. The rolls should be closely examined for erasures and alterations, and, where there are numerous records of "no sale" on the till-rolls, explanations should be sought.

TIME RECORDS.

(See ORGANISATION OF AN ACCOUNTANT'S OFFICE.)

TIME SHEETS.

(See COST ACCOUNTS, p. 349.)

TITHES.

Originally the rendering of one-tenth of the produce of the soil for certain religious purposes, but which have since been commuted by modern legislation into a yearly money payment dependent upon the average price of wheat for the preceding seven years. Tithes were formerly payable directly by the tenant, but are now payable by the landowner. (See COMMUTATION.)

TITLE.

The evidence of the right, or the right itself, under which a person claims property as his own. Sir Edward Coke defined the word thus: "*Titulus est justa causa possidendi id quod nostrum est*," that is, the ground of acquiring, whether purchase, gift, or other method, the word *titulus* being distinguished from the *modus acquirendi*, such as the delivery or conveyance of a thing. (See also REQUISITIONS OF TITLE.)

TITLE DEEDS.

(See ABSTRACT OF TITLE; INVESTMENTS, VERIFICATION OF.)

TOOLS.

(See LOOSE PLANT AND TOOLS.)

TRADE BILL.

This is the name which is very frequently given to a bill of exchange when the consideration for the same is the price of goods sold and delivered, or the value of services rendered. The existence

of a consideration of this nature distinguishes the negotiable instrument from one which is merely an accommodation bill (*q.v.*).

TRADE CHARGES.

This term is usually applied to the general expenses of carrying on trade and to the establishment expenses of a merchant's business. A merchant's Trading Account should contain only the actual sales (less returns) and purchases (less returns) and the opening and closing stocks. Consequently, although the term "Trade charges" would imply that the expenses referred to form a charge against the Trading Account, actually they are charged against Profit and Loss Account.

The auditor must require the production of duly certified invoices, demand notes, renewal notices, insurance policies, and other documents in support of the items charged, and must satisfy himself that all trade charges incurred within the period have been properly brought to account, that all accruing liabilities are provided for, and that all payments in advance are carried forward, so that only an equitable and appropriate charge is made against the period's revenue.

TRADE CREDITOR.

A person to whom money is owing on account of transactions had with him in the ordinary way of trading, and may be on account of goods supplied, or for work done which is an expense to the business of the person owing.

TRADE DISCOUNT.

This is an allowance, by means of a percentage deduction, from the selling price of goods. It does not depend upon the prompt payment of cash; but operates in any event. Being merely the means by which a trader regulates and adjusts his selling prices, no detailed record of trade discount need appear in the books of account. The allowance should, therefore, be deducted upon the face of the invoice, in the case of goods purchased, and the net amount of the invoice only entered in the Invoice Analysis Book. In the case of sales, where it is the practice to enter full particulars of each sale in the Sales Day Book the trade discounts may be shown there as a deduction; but when the Sales Day Book is entered up from the duplicate of the invoice sent out and only records the customers' names and the net amount of sales, then the trade discounts will not appear in the book, being already deducted on the duplicate invoice slips.

The auditor should satisfy himself that the proper trade discounts have been deducted from all invoices for goods purchased, so that there shall be no inflation of purchases or trade creditors. He should likewise be assured that all trade discounts allowable by the concern have been

properly deducted from the sales, so that no unearned profits shall have been taken credit for, and no debts stated in excess of the sum they may reasonably be expected to realise. (See also PROFIT AND LOSS ACCOUNT, p. 792; DISCOUNT, RESERVE FOR.)

TRADE DOCUMENTS.

(See INVESTMENTS, VERIFICATION OF.)

TRADE-MARKS.

(See DESIGNS AND TRADE-MARKS.)

TRADE UTENSILS.

This term is usually applied to unfixed or loose utensils, which should be treated in the books of account in the same way as Loose Tools (*q.v.*). That is to say, that they should be re-valued from time to time and taken into account in the same way as stock-in-trade, until the actual rate of depreciation to which they are subject has been ascertained by experience; after which they may be capitalised and their value written down in accordance with the rate so determined.

The auditor should require the production of a schedule of utensils and should satisfy himself that the valuation has been properly made and that it is duly certified by a responsible official appointed for the purpose.

TRADING ACCOUNT.

In all trading concerns three principal statements have to be prepared when the proprietor or proprietors of the concern wish to ascertain the result of its operations during any period, and its financial position at the end of that period. These three principal statements are known as a Trading Account, a Profit and Loss Account, and a Balance Sheet.

A Trading Account is a statement of account prepared for the purpose of showing what is known as the "gross profit" of the transactions of a trading concern during the period embraced by the account.

Gross profit is the term applied to that part of the profit of a trader, whether a manufacturer or a wholesale or retail dealer, which accrues before it is charged with the expenses connected with the distributing and recording departments of the business. The gross profit as ascertained by the Trading Account when reduced by charges connected with the expenses of the distributing and recording departments necessarily incurred before the goods reach the customers, becomes what is known as the "net profit," and the method by which the gross profit is reduced to the net profit is explained in the article entitled PROFIT AND LOSS ACCOUNT. The final entry in a Trading Account is consequently the balancing entry which shows the amount of the gross profit unless, as seldom occurs, the transactions of the period have been financially so disastrous that the statement shows the sales have resulted in a loss before being charged with any of the expenditure appertaining to the Profit and Loss Account.

It is proposed to deal first of all with the preparation of a Trading Account containing those items which commonly appear on the debit and credit sides of the majority of Trading Accounts, and then make some reference to a few items which appear in a few special cases of Trading Accounts, or in statements which are the equivalent of a Trading Account.

Where a proper system of double entry book-keeping is in force, the Trading Account, in conjunction with the other statements referred to as the Profit and Loss Account and the Balance Sheet, is prepared from the Trial Balance. From the Trial Balance are first of all extracted the items which properly appertain to the Trading Account, leaving the other items in the Trial Balance to be exhausted first into the Profit and Loss Account and then into the Balance Sheet, as explained in the articles dealing with these two statements.

Before referring in detail to any of the items usually appearing in a Trading Account a few examples of Trading Accounts are here set out.

THE LUXURY HOTEL COMPANY, LIMITED

Dr.

TRADING ACCOUNT FOR YEAR ENDING 31ST DECEMBER, 19...

Cr.

	£	s.	d.		£	s.	d.
To Provisions	38,000	0	0	By Bedrooms	18,000	0	0
" Wine and Liqueurs	6,000	0	0	" Private Sitting Rooms	7,800	0	0
" Spirits	1,500	0	0	" Baths	500	0	0
" Ales, Stout, Cider, etc.	600	0	0	" Billiard Room	1,200	0	0
" Mineral Waters	1,200	0	0	" Restaurant	53,000	0	0
" Servants' Wages	7,500	0	0	" Wine and Liqueurs	14,000	0	0
" Balance being Gross Profit carried to Profit and Loss Account	45,200	0	0	" Spirits	2,500	0	0
				" Ales, Stout, Cider, etc.	500	0	0
				" Mineral Waters	2,500	0	0
	£100,000	0	0		£100,000	0	0

THE LOTHBURY COMPANY, LIMITED

TRADING ACCOUNT FOR YEAR ENDING 31st DECEMBER, 19...

Dr.	TRADING ACCOUNT FOR YEAR ENDING 31st DECEMBER, 19...								Cr.	
	£	s.	d.	£	s.	d.		£	s.	d.
To STOCK-IN-TRADE .				75,000	0	0				
„ PURCHASES—										
Balance of Ledger										
Account . . .	160,000	0	0					285,000	0	0
Less										
Returns outward .	2,000	0	0					3,000	0	0
				158,000	0	0				
„ WAGES—										
Balance of Ledger										
Account . . .	43,000	0	0							
Deduct										
Amount chargeable										
to Profit and Loss										
Account . . .	5,000	0	0					1,000	0	0
				38,000	0	0				
„ CARTAGE—										
Conveyance of Goods										
to Warehouse .				16,000	0	0				
„ BALANCE—										
Being Gross Profit										
carried to Profit and										
Loss Account .				63,000	0	0				
				£350,000	0	0				
								£350,000	0	0

THE LLANESTON COLLIERY COMPANY, LIMITED

TRADING ACCOUNT FOR YEAR ENDING 31st DECEMBER, 19...

Dr.	TRADING ACCOUNT FOR YEAR ENDING 31ST DECEMBER, 19...								Cr.
	£	s.	d.	£	s.	d.	£	s.	d.
To Stock of Coal in Hand				8,000	0	0			
" WAGES—									
Overhead . . .	3,500	0	0						
Underground . . .	48,000	0	0						
				51,500	0	0			
" Dead Rents . . .				400	0	0			
" Royalties . . .				5,700	0	0			
" Timber . . .				4,400	0	0			
" Horse Account . . .				2,600	0	0			
" Stores . . .				4,300	0	0			
" Coal Cutting Expenses				2,500	0	0			
" Depreciation of Under-ground Plant . . .				4,000	0	0			
" BALANCE—									
Being gross profit carried to Profit and Loss Account				98,600	0	0			
				£182,000	0	0			
							£182,000	0	0

MESSRS. CADIZ & COMPANY

Dr.

TRADING ACCOUNT FOR YEAR ENDING 31ST DECEMBER, 19...

Cr.

	£	s.	d.	£	s.	d.		£	s.	d.	£	s.	d.
TO STOCK-IN-TRADE				19,650	0	0	By SALES						
„ PURCHASES—							(Details as on debit side if wished)	12,200	0	0			
Port	2,200	0	0				Less						
Sherry	800	0	0				Returns	400	0	0	11,800	0	0
Burgundies	1,200	0	0										
Clarets and Hocks, etc.	800	0	0				„ STOCK IN TRADE				26,200	0	0
Champagne	2,700	0	0										
Spirits	1,600	0	0										
Liqueurs	400	0	0										
				9,700	0	0							
„ DUTIES				2,400	0	0							
„ CELLAR WAGES				560	0	0							
„ BOTTLES, CORKS, Etc.				2,740	0	0							
„ FREIGHT AND CARRIAGE				300	0	0							
„ BALANCE						0							
Being Gross Profit				2,650									
				£38,000	0	0					£38,000	0	0

SALES.—The principal item which appears on the credit side of the Trading Account of any trader, whether wholesale or retail, is the amount of sales for the period, and although this would probably be shown in the balance of only one Ledger Account in the Trial Balance it is necessary to carefully consider what items should be included therein. It would not be safe either for the accountant who prepares the Trading Account from the Trial Balance, or for the auditor who has to audit the statement thus prepared, to conclude his duties without making a special investigation as to how the amount taken credit for in respect of sales has been arrived at in the Ledger from which the balance has been transferred to the Trial Balance.

The amount taken credit for in the Trading Account under the heading of “sales” may be divided into four classes—

1. Sales for cash during the period.
2. Sales on credit which have been paid for between the date of the sale and the date up to which the statement is prepared.
3. Sales on credit during the period payment for which had not been received at the date at which the statement is prepared.
4. Sales properly belonging to a period anterior to the period embraced by the Trading Account, but which have been omitted from previous Trading Accounts.

In order to ensure that the cash received for sales during the period has been included, the constructor of the Trading Account must inquire into the system of book-keeping in connection with the recording of the cash sales, and satisfy

himself that the full amount of cash received has been accounted for.

In many manufacturing concerns, and also in many wholesale houses where goods are only sent to retail traders, no sales are made for cash, and all sales are entered in the Day Books and posted therefrom to the debit of the Ledger Accounts of the buyers. The following remarks consequently apply only to trading concerns which sell to the public or perhaps to some who sell for cash to retail traders in a small way of business.

Cash taken over the counter in a large concern by the salesmen themselves, and cash received by a number of cashiers, is recorded first of all by each salesman entering in a manifold book, in triplicate, a short memorandum of the goods sold by him, and the price. The top memorandum is really the account itself, and is handed to the customer, the second one is torn out, and either filed by the salesman himself, if he takes the cash in payment, or by the cashier to whom either the salesman or the buyer has to present this account, the third being retained in the manifold book as an additional check.

Where money is paid to a cashier, in addition to filing the duplicate account handed to him, he has to enter the amount of the cash in a Cash Sales Book, as it is very important that the receipts by a cashier in respect of cash sales should be recorded separately from cash received by him in respect of sales for which credit has been given. In many large establishments a cashier who takes money for cash sales is not allowed to receive cash in payment of ledger customers' accounts.

The accounts filed by the cashier or by a salesman are collected periodically during the day, and are again entered in Cash Sales Books in the book-keeping department, so that the total amount received in respect of cash sales and of credit sales by each cashier during the day can be made up at the close of business. In the case, therefore, of any discrepancy, the books of a cashier whose cash handed over does not agree with the total amount shown in the books of the counting house as being due from him can be especially examined.

The total amount received during the day in respect of sales for cash should be paid into the bank under that heading, and posted through the Cash Book to the credit of "Cash Sales" in the Ledger; the total of which at the balancing of the books will either appear as a separate heading in the Trial Balance under "Cash Sales," or can be incorporated in one ledger account, and be taken therefrom in one item into the Trading Account.

As regards sales on credit, these will naturally be entered in a Day Book or Day Books, the amount of each sale being posted to the debit of the customer, while the total sales for a day, week, or month, according to the size of the business, should be posted to the credit of "Sales" in the Ledger. This applies to both sales on credit which have been paid for on or before the date of closing the books, and those which will not have been paid for at that date.

The amount due from customers who have not paid for the goods purchased by them at the date of the closing of the books will appear in the Balance Sheet under the heading of "Debtors," and a very important question arises in the preparation of the Trading Account as to the amount to be taken credit for in respect of sales on credit during the period which have not been paid for at the date on which the accounts are made up.

In order to arrive at this amount, the compiler of the Trading Account should go carefully through the Ledger Accounts of the debtors, and where he notices that a debtor has been irregular in his payments, more particularly in those cases where he is distinctly in arrear, he should call the attention of one of the partners or the manager of the company, as the case may be, and obtain his views as to the possibility of any loss arising on the realization of the total amount standing to the debit of this customer. Unless he compiles a list of the amounts which it is anticipated may not or will not be received, and pass a Journal entry debiting the sales with this amount, and crediting a Reserve which will ultimately either be deducted from the debtors taken credit for in the Balance Sheet, or treated as a Reserve on the liability side of that statement, the amount of sales taken credit for in the Trading Account will be too

large. Should any of the debtors become bankrupt or make an assignment, or in the case of a company, go into liquidation, either the compiler of the Trading Account or a responsible official should ascertain from the trustee or liquidator, as the case may be, the amount likely to be ultimately recovered, and treat the balance as part of the Reserve above referred to.

As regards the fourth class, or sales properly belonging to the period preceding the date of the commencement of the period embraced by the Trading Account, which may or may not have been paid for during the period of the current Trading Account, and which ought to have been taken to credit in the preceding Trading Account, such sales must necessarily be brought into the following account. It is advisable, however, that the amounts should be shown separately, as otherwise any comparison between the total sales of the two periods would be wrong and also any comparison of the percentage the gross or net profit bears to the sales of the two periods would also be wrong and consequently misleading.

The compiler of the Trading Account must be careful not to include among the sales goods sent out on consignment account, in other words, goods which are sent to accredited agents or representatives of the trader at the risk of the consignor. The consignees of such goods are only liable to remit payment when the goods have actually been sold by them, and until advice has been received from the consignees that the consignment has been sold, the value should not be taken credit for in the Trading Account under the heading of "Sales," but should be included under the heading "Stock-in-Trade" or appear separately as "Stock on Consignment," in both cases at or below cost price.

Unless the compiler of the Trading Account is careful, he may find, in those cases where the ledgers have not been properly kept, that the consignees have been debited with the amount of the consignments, or perhaps one or more of the consignments, and thus be brought in as an apparent debtor on the Trial Balance, while the goods themselves may, by mistake, have been included in the Day Book amongst ordinary sales. It is clear that where mistakes of this kind occur, that the sales of the period are unduly swelled, and if the goods on consignment are eventually sold, the Trading Account of the period in which the sale actually takes place will not receive the credit, and comparative statements will be rendered inaccurate.

STOCK-IN-TRADE.—The value of the stock-in-trade on hand at the close of business on the balancing day, must be inserted on the credit side of the Trading Account. Even where the nature of the business enables the concern to be worked with a very small stock on hand, it is of

importance that the proper value should be assigned to this stock.

In many trades, however, and, in fact, in the majority of trades, the value to be placed on this stock is of the utmost importance, and it is no exaggeration to state that it is practically possible in businesses where the stock is considerable to augment or decrease the profits of a concern by means of the value placed upon this stock and thus show any result which the owners or controllers of a concern may desire.

It follows, therefore, that it is of the greatest importance to define the basis for settling the values to be placed on the stock, and practically all professional accountants and business men are agreed that the true figure to be inserted is that which represents the cost price of all stock which has not depreciated in value, with an allowance or deduction in respect of that portion which may have depreciated since its purchase. The reason for deciding upon this method of arriving at the value may be easily explained. If the stock has appreciated in value since its purchase, and on that ground the value taken into the Trading Account is in excess of the cost price, the accounting period in which this particular stock, or portion of it, is sold would be deprived of the profit really earned during that period. In other words, the appreciation in value in the account would be forestalling the profits which has not really been earned. There is again also the chance that between the closing date of the Trading Account and the date on which the stock may be sold a fall may occur in the particular market, and in that way the Trading Account of that period will lose the benefit of the profit, if any, above that of the cost price, and the profit of the preceding period will have been unduly enhanced.

The aim, therefore, of any one preparing a Trading Account is to take all possible steps to ensure that the value of the good and marketable stock at the closing date of the Trading Account, shall not exceed the cost price.

In the case of stock which may have depreciated in value, this depreciation may have arisen from one or more of several causes. Many classes of stock depreciate in value from the mere result of time alone, such as chemicals, etc., others simply through weather, being either too hot or too cold, or through dampness. Other stock, although absolutely in as good a condition as when purchased, may depreciate in value through change of fashion, such as materials for clothing, and more especially in made up goods of millinery and dressmaking establishments. Again, other goods which have been laid in under normal circumstances to supply certain trades may become practically valueless owing to some new invention.

Whatever the cause may be, it is the duty of

any one preparing a Trading Account to go carefully into all these matters, and after having carefully arrived at the actual cost price of every item of the stock-in-trade, make use of such information as may be at his disposal, and deduct from the cost price such a sum as in his opinion would reduce the stock to such a figure as, if it had to be acquired on the date of the Trading Account, would be the proper price to give for it.

It therefore follows that the preparation of the inventory of the stock itself for the purpose of arriving at the figure to be inserted in the Trading Account is, in the case of most traders, a very important part of his annual work. In order that as accurate a result may be arrived at, it is advisable that the preparation for the taking of the inventory of the stock should be begun in ample time prior to the closing date, as it is always more difficult, no matter what care may be taken, to make a correct inventory—and in some cases it is absolutely impossible—after the date has passed.

The preparation varies according to the class of stock and according as to whether it is to be taken principally in bulk, by measurement, or by weight, or, as in many cases, a combination of all.

STOCK IN TRANSITU.—The treatment of this item will depend on whether or not the invoices for the goods in transit have been incorporated in the accounts. If the invoices relating to such goods have been entered in the Purchase Book, then the value of the goods in transit must be included in the Trading Account either as a separate item or as an addition to the value of the closing stock. If, on the other hand, the invoices have not been passed through the books, the goods in transit must be omitted from the Trading Account.

WINE MERCHANTS' STOCK-IN-TRADE.—There is one exception to the general rule that stock ought never to be taken into the Trading Account above cost price, and that is in the case of the stock of a wine merchant. It is a recognised fact that with a few occasional exceptions wine improves by age up to a certain point. The length of time during which the improvement takes place varies to a great extent on the strength of the wine. It is also a fact that owing to the different manner in which port is "made" it arrives at maturity at a far earlier age than was the case a quarter of a century ago, and consequently arrives at its best at an earlier date and deteriorates at an earlier date. It is therefore considered quite proper that for the purposes of stock-taking a certain amount may be added to the cost price of good vintage wines, but this increase must not be such as to raise the stock-taking price above that at which the wine merchant would have to acquire the same stock from a shipper.

When a few years ago, vintage port after being bottled, say, three years after vintage, cost 30s. per dozen, that same port was frequently saleable in ten years' time at either double or even three times the value. It might press very hard on a wine merchant who chose to limit his drawings from his business to the amount of profit shown by his accounts were this stock to remain at the cost price, and credit only be taken for the increase in value when the same was realized. It is therefore quite proper for an addition to be made annually to each dozen of wine, calculating the value of the stock in those cases when the wine is known to be gradually improving by age.

In the same way, when any wine is known to be deteriorating either by age or for any other reason, the value to be taken credit for in the Trading Account should be below the cost, and should not exceed the price the wine merchant would be prepared to purchase it for adding to his stock.

PURCHASES.—The principal item on the debit side of every Trading Account, except in the case of manufacturers, comes under the heading of "Purchases." In addition to including the amounts standing under that heading in the Trial Balance, the constructor of the account has to take proper precaution that the item includes the amount of the actual purchases made during the period, quite irrespective as to whether or not they have been paid for. He should, therefore, make full inquiries of the official who has charge of the department and also of the official who receives the invoices, and whose duty it is to enter them up in the Invoice Book, or whatever the book may be styled, so as to guard against there being no omissions. Should his experience extend over several years, he might take advantage of this experience by comparing the total amount of the purchases for each month during the period with the corresponding month of the previous year, more especially during the last month of the period, as it is against the omission of entries in connection with purchases made just before the date of the closing of the books that the constructor of the Trading Account has specially to guard.

It follows that the amount to be charged under the heading of "Purchases" must necessarily include the total amount due to creditors, both on open account or in respect of bills payable, which will appear in the Balance Sheet.

As for the purposes of comparison it is absolutely essential that the amounts charged for purchases during each period should strictly include only the actual purchases for the period, it is desirable that should it have been discovered during the current period that some purchases had been omitted from the accounts of the preceding period, the amounts should be taken out

separately and stated under a sub-heading in the accounts being dealt with, as otherwise the comparison of the percentage the gross profits of the two periods bear to the sales would be misleading.

The purchases should only include those goods acquired for the purposes of re-sale, and should not include goods which are to be made use of in other ways, such as the furniture for an office or warehouse, fixtures, plant, machinery, or workmen's tools. Furniture purchased by a furnishing company for the purposes of re-sale would naturally appear under Purchases Account, but articles of furniture acquired for use in an office or a warehouse would appear under a separate heading such as "Furniture," and not be charged against the Trading Account, but be transferred to the credit side of the Balance Sheet.

RETURNS.—In practically every trading concern certain of the goods which have been dispatched to the buyers and charged in the Day Books are returned by the customers on the ground that they are not exactly as ordered. Through misunderstanding or carelessness, goods are frequently sent in excess of the order, or not in accordance with sample, or in consequence of the goods ordered not being in stock, the nearest substitute has been dispatched, and not approved of by the purchaser. Goods also are sometimes damaged either before they leave the warehouse or in transit, and are sent back. It is the practice on the receipt of such goods by the seller for a "Sales Returned" Account to be debited in his ledger, and the customer's account credited, quite apart from any question which may arise between the parties as to whether the return was justifiable.

In the preparation of the Trading Account many firms charge the total amount of the "Sales Returned" Account for the period in the debit side of the Trading Account, while others deduct the amount from the sales on the credit side, leaving what may be described as the net amount of the "Sales" on the credit side.

This is distinctly the preferable way, as it shows the real amount of sales for the period, and moreover, it is also better for the purpose of comparing the total of the sales of one period with the total of the sales of another period. It is also better for calculating the percentage the gross profit of any period may bear to the sales, and the comparison of such percentage with the percentage of an earlier or later period are distinctly useful.

It is true this is a very simple calculation for any one to make, by deducting the amount of the returned sales on the debit side from the total sales on the credit side; but it is better that the net result should be shown on the face of the account.

WAGES.—The wages paid to all workmen in connection with the process of manufacture as distinct from wages of workmen connected with the distribution or delivery of goods to purchasers are charged in the Trading Account. In those cases where workmen are employed in connection with the manufacture and also in connection with the distributing and counting-house work, an analysis should be made of the wages. This is usually calculated on time sheets, on which should be shown in columns the number of hours occupied by each workman in connection with the two departments. The proper proportion can then be charged against the Trading Account, leaving the balance to be charged against the Profit and Loss Account. Although errors made in the apportionment would not affect the net profits of the concern, it is important that the calculations should be as exact as possible, so that the gross profit on the Trading Account can be correctly arrived at.

FREIGHT.—The Trading Account should also be charged with the entire cost in connection with the admission of goods into the warehouse. As a rule, goods are delivered free into the warehouse of the purchaser or to the nearest railway station, but when the purchaser has to bear any of the cost of transit it is chargeable against the Trading Account, and not against the Profit and Loss Account; in other words, where freight for goods from abroad, or carriage by railway, motor, or horse vehicles has to be paid by the purchaser, the whole of these expenses, including any amount due at the date of the closing of the books should be charged against the Trading Account.

This class of expenditure is necessarily looked upon as part of the actual purchase price of the goods, and, therefore, has to be taken into consideration before the gross profit is ascertained.

DEAD RENT.—In mining concerns, including collieries, it frequently occurs that the property being mined is held on lease under the terms of which a fixed minimum rental is paid to the landlord should the royalties not equal in amount that of the Dead Rent. The compiler of the Trading Account should, as a rule, charge the full amount of the Dead Rent in the account he is preparing where the royalties fall short of that amount. As, however, there is usually a provision in the lease that this Dead Rent may be recouped out of royalties payable in future years, this must be taken into consideration. In the early state of the development of a mine it may be allowable not to charge the Dead Rent in the expectation that in the next few years the royalties will be of sufficient amount to cover the Dead Rent apportionable among the preceding years, and should an income be derived from ores raised during this early period, it would press unduly hard on these years were the whole of the Dead Rent to be charged to this. Discretion, however, must

be exercised in omitting to charge the Dead Rent, and the mining engineer should be consulted and, if possible, an estimate be obtained from him as to the amount of dead rent which in his opinion should be included among the expenditure.

ROYALTIES.—Referring to the preceding item "Dead Rent," the lease to a mining concern usually contains a clause whereby the ground landlord is entitled to a sum payable on a certain fixed quantity of mineral extracted from the ground. This sum may be either calculated per ton raised, or persquare yard cut, as the case may be. Amounts vary considerably in various districts and countries, and the compiler of the Trading Account must be careful that the full amount of royalty should be charged in his statement. For that purpose he should ask to be provided with the periodical statement of the superintendent of the mine or colliery, as the case may be, and also the account of the landlord's surveyor. The amount chargeable has nothing whatever to do with the quantities sold, as it is calculated on the quantity of mineral raised from the mine. Should dead rent have been charged in previous periods which is recoupable out of these royalties, the amount of the dead rent so recoupable must be deducted from the amount of royalty charged before the account is settled.

DEPRECIATION.—In the case of a manufacturing concern where machinery is employed, and where the workmen use a number of loose tools as apart from the machinery, it is the practice to charge the Trading Account with what is called "Depreciation," or a sum equivalent to the wear and tear of the machinery and tools employed. The amount is usually arrived at by charging the Ledger Account or accounts under which the plant, machinery, etc., is classified with the cost of additions to the plant, machinery, etc., and crediting the account or accounts by debiting the Trading Account with what, in the opinion of the proprietor of the business or directors of the company, guided by their expert, such as their engineer, may decide on the proper proportion to write off for the period, and charge it against the Trading Account.

As this is so fully dealt with in the article on DEPRECIATION, it is not necessary to enlarge upon it here, but the compiler of the Trading Account must bear this item in mind, and when arriving at his amount must carefully consider the subject from various points. Not only should the exact amount representing wear and tear be charged, but in many cases there has to be taken into consideration as to whether the introduction of some new class of machinery may not have shortened the ordinary duration of the life of the machinery in use at the present time, or if there is any reason to suppose that the existing machinery will have to be entirely replaced, and

a correspondingly heavier amount written off and charged against the Trading Account than has been the practice hitherto.

GENERAL REMARKS.—It is the practice of many trading concerns to charge against the Trading Account, before carrying a balance to the Profit and Loss Account, a certain proportion of every expense before arriving at the gross profit.

When the business of a concern is carried on at a warehouse, under a different roof to that of the counting-house, it is the practice of many concerns to charge against the Trading Account the rental and the expenses in connection with it, such as taxes, rates, heating, lighting, and water, and in those cases where the warehouse department is carried on under the same roof, to charge a proportionate part of such expenditure as may be deemed applicable to the trading department. In the former case the constructor of the Trading Account has no difficulties beyond ascertaining that all the outstandings at the end of the period are included. In the latter case, he should either himself make or obtain from some properly appointed official a schedule of the total expenditure, with columns showing the amounts to be charged to the Trading Account, and the amounts to be charged against the Profit and Loss Account, and he should satisfy himself that this has been done on a sound and equitable basis. Where the accounts are kept on a sound costing system the compiler of the Trading Account will have little difficulty in ascertaining the true gross profit.

When the draft Trading Account has been practically settled it would be as well to supply a test, in order to guard against the omission of any liabilities in connection with the purchase of stock. The test suggested is to ascertain the percentage the gross profit bears to the turnover or sales, and compare it with the percentage of the gross profit earned in the preceding few years.

In making this test the compiler must be careful that the statements submitted for comparison have been prepared on exactly the same basis; as otherwise the percentages will be misleading.

If it be found that the percentage of gross profit for the year is much higher than that of the preceding year, or the two years, or the average of the past, say, three, four, or five years, the compiler should consult a partner or official of the company, as the case may be, most acquainted with the business, and ascertain if he can account for it. If he cannot do so to the satisfaction of the compiler, it may point to stock having been taken credit for at the expiration of the period the invoices for which had not been included in the Purchases Account, and this is by no means of infrequent occurrence.

The balance shown by the Trading Account can then be transferred by the compiler to the Profit

and Loss Account. With very rare exceptions it is carried to the credit side, and is usually known among accountants as the gross profit. As explained in the article on the PROFIT AND LOSS ACCOUNT, it is reduced in that account by the charging of office and general expenses to what is known as the net profit. Occasionally, as has been already stated, but very rarely, the Trading Account may result in a loss which has to be carried to the debit side of the Profit and Loss Account, but this only occurs in those cases where there has been a considerable fall in the price of the articles sold. The loss may have been made on the purchase and sale of articles acquired during the period, or such a fall in the value may have occurred that many of the articles included in the "Stock-in-Trade" at the end of the period are taken into stock at lower prices than they were taken credit for in the stock-taking of the previous period.

If a robbery of stock has taken place during the period this would naturally affect the gross profit, and might affect it to such an extent as to leave a loss on the Trading Account, but in the majority of cases the Trading Account results in a profit. (See ACCOUNTS, CRITICISM OF, p. 12; INVESTIGATIONS, p. 574; PROFIT AND LOSS ACCOUNT, pp. 784 and 787; TRADING ACCOUNTS, APPROXIMATE.)

TRADING ACCOUNTS, APPROXIMATE.

Trading Accounts prepared before the balancing is fully completed, but when it is in such a condition that the results are known to be approximately correct.

TRAFFIC RECEIPTS.

(See PROFIT AND LOSS ACCOUNT, p. 788.)

TRANSFER OF A BILL BY DELIVERY.

By transfer is meant the passing of the property in anything by one person to another, and a distinction is made between "transfer" and "transfer by delivery" in that the latter signifies the physical act of passing. In the case of a bill of exchange the transferor may, if the bill has been indorsed to him in blank, transfer the same without signing the instrument. This does not happen very often, because the value of a signature is such that no one cares to have a negotiable instrument unless authenticated by the signature of a transferor, seeing that unless there is a signature the transferor cannot be sued upon the bill. If, however, there is a mere transfer by delivery, and the bill is not paid in due course, although the transferor cannot be sued on the bill, he may be liable in an independent action for breach of

warranty. What a transferor by delivery warrants to his immediate transferee, being a holder for value, is that the bill is what it purports to be, that he has a right to transfer it, and that at the time of the transfer he is unaware of any fact which renders it a valueless document. The added importance of seeing the signature of the transferor will be perceived when it is pointed out that not only is he not liable on the bill if his signature is not there, but he is not liable in an independent action upon the consideration in respect of which he transferred the bill, in case the bill should be dishonoured unless (1) the bill was given in respect of an antecedent debt, or (2) it appears that the transfer was not intended to operate in full and complete discharge of such liability.

TRANSFER FEES.

(See AUDITING, p. 78; PROFIT AND LOSS ACCOUNT, p. 788.)

TRANSFER JOURNAL.

(See SELF-BALANCING LEDGERS, p. 851.)

TRANSFER OF SHARES.

(See SHARES, TRANSFER OF.)

TRANSFERS.

It is often essential that items should be transferred from one ledger to another, as in the case of (a) items posted to an incorrect account; (b) alteration of decision as to method of treatment; (c) bad debts; (d) " Contra " Accounts, when separate accounts are kept in the Debit and the Credit Ledgers, and the matter is settled by payment of the balance between the accounts; (e) when instructions are received from a person owing money to the firm, to charge a person to whom the firm is indebted with the whole or part of his account, the arrangement being, of course, corroborated by the creditor.

These are known as transfers, and for their record a separate Transfer Journal is sometimes kept, having columns for each Ledger. The one given under "Columnar Journals" is ruled for this as well as general purposes, but when a separate Journal is used, the form given hereunder may be adopted—

TRANSFERS OF SHARES, AUDIT OF.

Where there is employed a registrar, the work of auditing transfers of shares, stocks, and debentures is sometimes performed by the secretary, and sometimes by the accountant, or the auditor of the company.

The auditor should check the entries in the Register of Transfers in conjunction with the deeds, the latter being examined with the object of seeing that they are properly stamped, dated, signed and attested, that the number of shares transferred and their respective distinctive numbers are in order, and that the deeds are otherwise complete and correct. He should see the relative certificates to the transfers, and verify the latter with the accounts in the Share Register.

The new certificates having been prepared for sealing and signature by the Board, he should check these with the actual transfer deeds, as well as all balance certificates, and his report will probably be in the following phraseology—

I beg to inform you that I have examined-----
Transfer Deeds numbered-----to-----, the
new certificates numbered-----to-----in relation
thereto, and report that they are correct, and that the
latter may be sealed and signed.

I have seen that the old certificates to which the transfers relate are duly cancelled.

The auditor should mark in a distinctive manner all documents seen and passed.

The work of auditing transfer forms no part of the ordinary audit of a company's accounts, and is usually remunerated at a rate per transfer.

TRAVELLERS' COMMISSION.

A convenient method of ascertaining and recording commissions due to travellers is that of adding to the Sales Day Book several analytical columns, in which the sales arising from orders secured by the various travellers are appropriately analysed. The periodical totals of the analysis are summarised in a Travellers' Commission Book, and the amount of commission due calculated therefrom. The book then forms the basis of

TRANSFER JOURNAL

[illegible]

the Journal entry crediting the travellers' personal accounts and debiting the Commission Account.

This book should be tested by the auditor, who should also have reference to the service agreements which fix the terms and rates of the commission payable, and from which he can satisfy himself whether or not the proper amount of commission has been charged against revenue.

In cases in which commissions are payable only when the value of the sales effected has been received, a reserve should be made in respect of travellers' orders executed but not paid for at the time of closing the books.

It is usual to provide in service agreements that no commission shall be payable in respect of sales which ultimately prove to be bad debts. The auditor should, therefore, see that the bad debts, and returns and allowances, are deducted from the appropriate total sales before the commission payable is calculated.

TRAVELLING EXPENSES.

Travelling expenses should be recorded in detail in a separate book kept for that purpose, and receipts should be given in every instance by the persons receiving the expenses. The book will then form the voucher for the appearance of these items in the Cash Book. It is advisable that separate Travelling Expenses Accounts should be kept in respect of each traveller, and the accounts, or the Travelling Expenses Book, should be regularly examined, and, if approved, initialed by a director or other responsible official.

The auditor should examine the Travelling Expenses Book carefully, and where any fixed scale of expenses is in existence should compare the scale with the records in the book, to see that the scale has not been exceeded. He should note that the book, or the individual ledger accounts, have been properly approved. By way of a test, he should compare the total of each traveller's Expenses Account with those of previous corresponding periods, and seek an explanation of any increase of moment. Such increases may be explained by the fact that the traveller's area has been enlarged and, consequently, greater expenses have been incurred.

TRIAL BALANCE.

A statement of the balances standing in the books for the purpose of testing the accuracy of the entries. Thus, all debit balances being placed in the debit column, and all credit balances in the credit column of the Trial Balance, the totals of such abstracted balances should agree.

TRIPARTITE.

The meaning of this word is, "composed of three parts or parties." Any agreement entered into which consists of three parts is so called.

TRUE YIELD.

A term of common application to the income derived from investments, usually expressed in terms of a percentage, *e.g.* a 6 per cent. stock quoted at £90, represents a net yield of 6.66 per cent. $\left(\frac{100 \times 6}{90}\right)$.

If the stock be definitely redeemable, say in four years at 100, or par, there would be a profit of 10 points, using the usual terminology, in four years, or $2\frac{1}{2}$ points per annum, thus giving, as it is frequently stated, an additional $2\frac{1}{2}$ per cent. per annum; so that the return, including redemption, is 9.16 per cent. This method is, however, obviously incorrect.

Let us assume a 6 per cent. bond purchased for £90 and redeemable in four years at par—interest payable half-yearly. The true yield is, from inspection, between 9 and 10 per cent. It is 4.5173 per cent. per half-year, and the accounts, limiting the decimals, are as under—

BOND ACCOUNT			
To Cost of Bond	£ 90	By Cash on Redemption	£ 100.00
" Interest A/c	1.06		
" Do.	1.11		
" Do.	1.17		
" Do.	1.22		
" Do.	1.27		
" Do.	1.33		
" Do.	1.39		
" Do.	1.45		
	£ 100.00		£ 100.00
INTEREST ACCOUNT			
To Income Account	£ 4.06	By Cash	£ 3.00
		" Bond Account	1.06
	4.06		4.06
To Income A/c	4.11	By Cash	3.00
		" Bond A/c	1.11
	4.11		4.11
To Income A/c	4.17	By Cash	3.00
		" Bond A/c	1.17
	4.17		4.17
To Income A/c	4.22	By Cash	3.00
		" Bond A/c	1.22
	4.22		4.22
To Income A/c	4.27	By Cash	3.00
		" Bond A/c	1.27
	4.27		4.27
To Income A/c	4.33	By Cash	3.00
		" Bond A/c	1.33
	4.33		4.33
To Income A/c	4.39	By Cash	3.00
		" Bond A/c	1.39
	4.39		4.39
To Income A/c	4.45	By Cash	3.00
		" Bond A/c	1.45
	4.45		4.45

INCOME ACCOUNT

By Interest A/c . . .	£	4'06
" Do.	"	4'11
" Do.	"	4'17
" Do.	"	4'22
" Do.	"	4'27
" Do.	"	4'33
" Do.	"	4'39
" Do.	"	4'45

It will be seen that the premium on redemption is dissipated during the tenure of the bond.

TRUST ACCOUNTS.

(See EXECUTORSHIP ACCOUNTS.)

TRUST AND FINANCE COMPANIES, AUDIT OF.

(See AUDITING, p. 109.)

TRUSTEE.

A trustee is the person to whom property is entrusted in order that the same may be dealt with in accordance with the directions given by the creator of the trust. The person for whose benefit a trust is created is called the *cestui que trust*. If there are more persons than one who are beneficiaries, they are called *cestuis que trustent*.

Generally speaking, trustees are appointed by the instrument which creates the trust, whether that instrument is a deed or a will, and in all properly drawn documents provision is made for supplying the places of trustees who die or wish to retire. But if this important matter of appointment has been overlooked, the trust does not, therefore, fail. If the Court is satisfied that there is a trust in existence, it will itself appoint a trustee or trustees to carry the same into effect. This is an essential matter, because no person is compelled to accept the office of trustee any more than he can be forced to act as an executor. Any person who has been appointed can disclaim even by word of mouth; but it is always advisable that a disclaimer should be made in writing. If, however, a person who has been named as trustee intermeddles with the property, his right of disclaimer has gone. Matters have been much simplified in modern times by the appointment of a judicial trustee or by entrusting the administration of the estate to the Public Trustee.

It is impossible in the space at disposal to enter into the multifarious matters concerning trustees generally. If the creator of the trust appoints particular individuals, it will require a very strong case to remove them from the office, if they once act. The creator has expressed his confidence and that is, ordinarily, quite sufficient. In carrying out their duties, trustees ought to be guided by the instrument which invests them with these powers. They must, first of all, reduce the subject matter of the trust into their possession, and then they must use all that care which an average business man would exercise in the transaction of

his own business. As to investments, they must follow the directions of the trust deed or will, and if there are no directions, then their duty is to keep well within the limits of those investments permitted by law. (See TRUSTEE INVESTMENTS.) It is needless to say that they should keep strict accounts, and at the termination of the trusteeship they must be able to show how every penny derived from the estate has been expended. When cases of difficulty or doubt arise trustees should not act upon their own responsibility; they should apply to the Court for directions or advice, which can always be done, if the case is reasonable, at the expense of the estate. The great aim is always to keep the *corpus* of the trust estate intact. Of course, the trust deed or will may allow the capital to be encroached upon for specific purposes, and certain statutes allow for advances being made in suitable cases. But trustees should never act unless upon the safest ground, and, as has been already mentioned, the advice of the Court should be sought in all cases of doubt. The income arising from the trust estate must be expended strictly in accordance with the terms of the trust, or of any statutory enactments which affect the same.

Trustees may reimburse themselves out of the trust funds in their hands for all expenses properly incurred by them, but unless otherwise directed by the instrument creating the trust, their services and office must be gratuitous. There must not be the slightest suspicion of any profit made or advantage taken through dealing with the trust property, directly or indirectly. For example, a sale of property to the trustee himself is always regarded with suspicion, and is likely to be impeached. Again, if trustees deal with the money of their *cestuis que trustent*, they are accountable for any profit made by them, and responsible for any loss which may arise. Also, if they mix trust money with their own, and any transactions take place with the mixed fund, it is the money of the trustee which is presumed to be utilised for the purpose, whilst the money of the *cestuis que trustent* is held to be intact, so long as there is sufficient left of the mixed fund to cover the same. By several recent statutes certain indemnities have been given to trustees in order to lighten the burdens placed upon them by judicial decisions. Thus, by the Trustee Act, 1893, in the case of signing receipts for conformity, a trustee is relieved unless a loss has arisen through his own act or wilful default. And where a breach of trust has been instigated by a *cestui que trust*, his interest can be impounded towards recouping the trustee. Again, by later enactments, where it appears to the Court that a trustee is or may be personally liable for any breach of trust whenever it occurred, but has acted honestly and reasonably and ought fairly to be excused for the breach, and for

omitting to obtain the directions of the Court in the matter in which he has committed such breach, the Court may relieve the trustee either wholly or in part from personal liability. But a prudent man will not rely on these indemnity clauses and powers of obtaining repayment or relief. He should in all cases act strictly in accordance with his duties, remembering that if a wrong is done he may have to bear all losses himself, for between wrong-doers there is no contribution, and the *cestuis que trustent* may claim against him alone, and leave out his co-trustee. If the friction between the different parties becomes great, the safest course for the trustee who disapproves of the contemplated breaches of trust to adopt is to take measures to have the trust funds paid into Court, and to free himself from the trust.

If a trustee desires to retire from a trust which he has undertaken, he can always do so, provided that there are two or more trustees left to carry on the same, or another is appointed to take his place. The greatest care must be exercised in seeing that the estate is not left in the hands of a single trustee.

When all the purposes for which a trust was created have been fulfilled, and before a final distribution of the property is made, the trustees should submit their accounts to the beneficiaries, and obtain a formal release from them. They are entitled to do this at the expense of the trust estate. The release should set out all that has been done in respect of the estate, and should be by deed.

A trustee of any property, whether for the use or benefit of a private person, or for any public or charitable purpose, is liable to be convicted of a misdemeanour and sentenced to penal servitude if he is found guilty of converting or appropriating any part of the trust property to his own use and benefit. No prosecution can be instituted without the consent of the Attorney-General. (See also EXECUTORSHIP ACCOUNTS.)

TRUSTEE ACCOUNTS.

(See BANKRUPTCY ACCOUNTS, pp. 186, 217.)

TRUSTEE IN BANKRUPTCY.

(See BANKRUPTCY, TRUSTEE IN.)

TRUSTEE INVESTMENTS.

A trustee or trustees must invest the trust funds which they hold in accordance with the terms of the deed or will under which they are appointed. In the absence of any direction, the Trustee Act, 1893, provides as to investments as follows—

"Section 1. A trustee may, unless expressly forbidden by the instrument (if any) creating the trust, invest any trust funds in his hands,

whether at the time in a state of investment or not, in manner following, that is to say—

"(a) In any of the Parliamentary stocks or public funds or Government securities of the United Kingdom;

"(b) On real or heritable securities in Great Britain or Ireland;

"(c) In the stock of the Bank of England or in the Bank of Ireland;

"(d) In India Three and a half per cent. stock and India Three per cent. stock, or in any other capital stock, which may at any time hereafter be issued by the Secretary of State in Council of India under the authority of Act of Parliament, and charged on the revenues of India;

"(e) In any securities the interest of which is for the time being guaranteed by Parliament;

"(f) In consolidated stock created by the Metropolitan Board of Works, or by the London County Council, or in debenture stock created by the receiver for the Metropolitan Police District;

"(g) In the debenture or rent charge, or guaranteed or preference stock of any railway company in Great Britain or Ireland incorporated by special Act of Parliament, and having during each of the ten years last past before the date of investment paid a dividend at the rate of not less than three per centum per annum on its ordinary stock;

"(h) In the stock of any railway or canal company in Great Britain or Ireland whose undertaking is leased in perpetuity or for a term of not less than two hundred years at a fixed rental to any such railway company as is mentioned in Subsection (g), either alone or jointly with any other railway company;

"(i) In the debenture stock of any railway company in India the interest on which is paid or guaranteed by the Secretary of State in Council of India;

"(j) In the 'B' annuities of the Eastern Bengal, the East Indian, and the Scinde Punjaub and Delhi Railways, and any like annuities which may at any time hereafter be created on the purchase of any other railway by the Secretary of State in Council of India, and charged on the revenues of India, and which may be authorised by Act of Parliament to be accepted by trustee; in lieu of any stock held by them in the purchased railway; also in deferred annuities comprised in the register of holders of annuity Class D, and annuities comprised in the register of annuitants Class C of the East Indian Railway Company;

"(k) In the stock of any railway company in India upon which a fixed or minimum dividend in sterling is paid or guaranteed by the Secretary of State in Council of India, or upon the capital of which the interest is so guaranteed ;

"(l) In the debenture or guaranteed or preference stock of any company in Great Britain or Ireland, established for the supply of water for profit, and incorporated by special Act of Parliament or by Royal Charter, and having during each of the ten years past before the date of investment paid a dividend of not less than £5 per centum on its ordinary stock ;

"(m) In nominal or inscribed stock issued, or to be issued, by the corporation of any municipal borough having, according to the returns of the last census prior to the date of investment, a population exceeding fifty thousand, or by any county council, under the authority of any Act of Parliament or Provisional Order ;

"(n) In nominal or inscribed stock issued, or to be issued, by any commissioners incorporated by Act of Parliament for the purpose of supplying water, and having a compulsory power of levying rates over an area having, according to the returns of the last census, prior to the date of investment, a population exceeding fifty thousand, provided that during each of the ten years last past before the date of investment the rates levied by such commissioners shall not have exceeded eighty per centum of the amount authorised by law to be levied ;

"(o) In any of the stocks, funds, or securities for the time being authorised for the investment of cash under the control or subject to the order of the High Court,

"and may also from time to time vary any such investment.

"2. (1) A trustee may under the powers of this Act invest in any of the securities mentioned or referred to in Section 1 of this Act, notwithstanding that the same may be redeemable, and that the price exceeds the redemption value.

"(2) Provided that a trustee may not under the powers of this Act purchase at a price exceeding its redemption value any stock mentioned or referred to in sub-sections (g), (i), (k), (l), and (m) of Section 1, which is liable to be redeemed within fifteen years of the date of purchase at par or at some other fixed rate, or purchase any such stock as is mentioned or referred to in the Subsections aforesaid, which is liable to be redeemed at par or at some other fixed rate, at a price

exceeding fifteen per centum above par or such other fixed rate.

"(3) A trustee may retain until redemption any redeemable stock, fund, or security which may have been purchased in accordance with the powers of this Act.

"3. Every power conferred by the preceding Sections shall be exercised according to the discretion of the trustee, but subject to any consent required by the instrument, if any, creating the trust with respect to the investment of the trust funds.

"4. The preceding Sections shall apply as well to trusts created before as to trusts created after the passing of this Act, and the powers thereby conferred shall be in addition to the powers conferred by the instrument, if any, creating the trust.

"5. (1) A trustee having power to invest in real securities, unless expressly forbidden by the instrument creating the trust, may invest and shall be deemed to have always had power to invest—

"(a) On mortgage of property held for an unexpired term of not less than two hundred years, and not subject to a reservation of rent greater than a shilling a year, or to any right of redemption, or to any condition for re-entry except for non-payment of rent.

"7. (1) A trustee, unless authorised by the terms of his trust, shall not apply for or hold any certificate to bearer issued under the authority of any of the following Acts, that is to say—

"(a) The India Stock Certificate Act, 1863 ;

"(b) The National Debt Act, 1870 ;

"(c) The Local Loans Act, 1875 ;

"(d) The Colonial Stock Act, 1877.

"8. (1) A trustee lending money on the security of any property on which he can lawfully lend shall not be chargeable with breach of trust by reason only of the proportion borne by the amount of the loan to the value of the property at the time when the loan was made, provided that it appears to the Court that in making the loan the trustee was acting upon a report as to the value of the property made by a person whom he reasonably believed to be an able practical surveyor or valuer instructed and employed independently of any owner of the property, whether such surveyor or valuer carried on business in the locality where the property is situate or elsewhere, and that the amount of the loan does not exceed two equal third parts of the value of the property as stated in the report, and that the loan was made under the advice of the surveyor or valuer expressed in the report."

By section 2 of the Colonial Stock Act, 1900, a trustee is empowered to invest in any colonial stock registered in the United Kingdom in accordance with the provisions of the Colonial Stock Acts, 1877 and 1892, as amended by this Act, provided such stocks have been notified in the *London Gazette* as having been approved by the Treasury, subject to the restrictions contained in Section 2, Subsection 2, of the Trustee Act, 1893.

It has been pointed out by a leading legal authority that the powers of trustees under an investment clause which authorises them to invest

the trust funds in such securities, or in such manner, as they think fit are not very clear, and that having regard to the state of the authorities it behoves trustees having such powers to be careful when they travel outside the securities authorised by law for the investment of trust funds.

The Trustee Act, 1893, in so far as it provides for investments of trust funds, has been amended from time to time, particularly by the provisions of war-time legislation, allowing investments in bonds, securities, etc., issued by the British Government for war purposes.

UBERRIMAE FIDEI.

THIS is a Latin phrase, the meaning of which is "of the utmost good faith." In ordinary contracts the law always requires "good faith," which is generally taken to mean an absence of anything in the nature of dishonesty, fraud, deceit, wilful misrepresentation, or a suppression of the truth. But in certain special contracts, of which insurance is the chief example, something more is required, namely, a most complete disclosure of every fact or circumstance connected with the matter which might in any way affect the mind of any of the parties to the contract. Nothing must be concealed, and if there is any suppression, however lawful it might be in the case of an ordinary contract, that is a sufficient ground for cancellation. Contracts in which this complete disclosure must be made are said to belong to the kind which are classified under the heading of contracts *uberrimae fidei*, e.g. Insurance.

UMPIRE.

In all matters which are referred to arbitration, it is the general practice for the parties to agree upon the reference being entrusted to two arbitrators, one to be appointed by each side. This may give rise to difficulties, as the two arbitrators may not be able to arrive at an agreement. To prevent the inquiry being abortive, there is often inserted in the terms of reference a clause to the effect that if the two arbitrators cannot agree, a third person shall be nominated by the two arbitrators to decide the points which are still left open. This third person is called the "umpire." (See ARBITRATION.)

UNCALLED CAPITAL.

(See BANKRUPTCY ACCOUNTS, p. 167 ; LIQUIDATORS, ACCOUNTS OF, p. 650.)

UNDER-LEASE.

This is a lease which is granted by a person who is himself only the lessee of the premises which he under-lets. Thus, if A grants a lease of land to B for a term of years, and B afterwards grants a lease for a less period than he himself holds of the same land to C, C holds the lease under an under-lease. In this respect an under-lease differs from an assignment, by which the original lessee transfers the whole of the term still existing in him. The under-lessee has no privity of contract with the original lessor ; his contract

is with the original lessee only, and he is bound to the lessee under the special terms of his sub-lease independently of anything which exists between the original parties to the lease.

UNDERWRITERS' ACCOUNTS.

Underwriters' accounts, though frequently relieved in their technicality by one or two peculiar features of interest, are "wearisome to a degree," and require the exercise of a considerable amount of care rather than of, inordinate skill. Instructions have been issued by Lloyd's Committee from time to time for the guidance of auditors, the work in connection with the accounts of the members of that body apparently being the monopoly of a select few.

The prescribed form of audit certificate (in duplicate words to comply with the requirements of the Board of Trade) is to be completed and signed after the examination of the books of the Underwriting Account and sent to Lloyd's Committee in March of each year.

The auditor must examine the premiums, claims, salvage recoveries and re-insurances, and agree the totals, his principal work, however, being in the Cash Book and the ledgers, such as checking the additions of the Cash Book, vouching the payments, checking the Cash Book with the Bank Pass Book and agreeing the reconciliation if one be necessary, checking postings, accounting for all dividends and interests on investments, checking the additions of the claims, re-insurance and salvage recoveries books, checking the postings to the impersonal accounts, checking the postings, additions and balances of the brokers' ledgers, seeing that the Underwriting Accounts are kept separate, and that the claims, salvages, and re-insurances are taken to their proper years.

A list of the investments with values at the 31st December, will be furnished, and bonds and certificates produced for verification as well as the Bank Pass Book and bank certificate of the bank balance on the same date. The auditor must compare the securities with the entries in the books and satisfy himself that such securities are correctly valued and have been, or are, held by the underwriters or their bankers free from any charge or encumbrance except for the purpose of the Underwriting Account. In cases where the investments are not easily realisable provision must be made for the necessary margin.

In auditing the accounts for 1920, say, the auditor must ascertain by inspection of the books

the percentage of settlements for the second and third years on the years 1916, 1917, and 1918, showing the probable cost of winding up the Underwriting Account. As regards the 1919 account the estimate of the third year's settlements is made by taking the average percentage of the third year's settlements in 1916, 1917 and 1918, and as regards the 1920 account the estimate for the second year's settlements is made by taking the average of the second year's settlements in 1916, 1917 and 1918, the estimates for the third year's settlements being similarly ascertained by taking the average of the third year's settlements in 1916, 1917 and 1918. In cases where the marine premium income exceeds £7,500 the percentages of settlement must be ascertained separately for Time and Voyage Accounts as shown by the books for the years 1916, 1917, and 1918, and the estimate must be made by taking the average settlements of the Time Account for these years for the Time Account and the Voyage Account for these years for the Voyage Account. If the accounts do not admit of this being done the auditor must apply to the committee for instructions. The amount required to wind up the 1919 and 1920 accounts (all claims on previous years being placed against the 1919 account), thus ascertained, is to be compared with the assets shown in the balance sheet as at 31st December, 1920, *i.e.*—

1. Bank balance. If cash is paid in to make up any deficiency the auditors must see that the amount has been paid in with the knowledge and assent of the name or names of the trustees to the deed to be retained or used by them for the purposes of the account.

2. Investments at market price on 31st Dec., 1920.

3. Broker's balances—credit less debit.

4. Lloyd's deposit and funds provided, at the price on the 31st December, 1920.

The auditor must ascertain by inspection of the books, the amount of the premium income for 1920 for non-marine risks, *i.e.* all risks except those upon—

Vessels of any description, including barges and dredgers, cargoes, freights, and other interests which may be legally insured by, in, or in relation to vessels, cargoes and freights, goods, wares, merchandise, and property of whatever description insured for any transit by land or water, or both, and whether or not including warehouse risks or similar risks in addition or incidental to such transit.

Where underwriters have made a special deposit for employer's liability risks, the accounts for such risks must be excluded from this audit and the amount of the premium income must be certified by inspection of the books.

It must be borne in mind that the Lloyd's deposits are only liable for the risks for which they are respectively provided, *viz.* (a) marine; (b) non-marine; (c) employer's liability. In cases where the certificate covers only a portion of the Underwriters' Account, *i.e.* where there is a separate office account or whether the underwriter is written for in other syndicates, the fact must be mentioned. The particulars of the Lloyd's deposits (marine, non-marine, and/or employer's liability) will be furnished to the auditor by the secretary of Lloyd's if required.

The auditor is required to certify that the books of the Underwriting Account have been examined in accordance with the instructions, and (except in those cases where the premium trust deeds are furnished in pursuance of the Assurance Companies Act, 1909, and are lodged with the Committee of Lloyds), that the underwriters have signed a premium trust deed in the form approved by the Committee of Lloyds. In cases where the re-insurances amount to 20 per cent. or more of the premium income, the auditor must satisfy the Committee that the re-insurance policies form a good asset before giving the certificate.

Where, in the opinion of the auditor, an abnormal balance is owing by any broker, the auditor must either satisfy himself that the asset is a reasonably good one or note the fact in his report for the information of the Committee.

UNDERWRITING AGREEMENTS.

Underwriting transactions are of common occurrence in company accounts, underwriting commission being a sum payable for guaranteeing the subscription either in whole or in part to an issue of shares or stock, and debentures or loans, expressed usually in terms of a percentage. It may be payable either in cash or in kind, partly in one and the other; and on these points the auditor should notice the conditions of the agreement, and in the case of a limited company the articles of association to see that the authority and rate and measure of satisfaction are in order. In practice commission is often paid to underwriters and sub-underwriters, and there is also paid over-riding commission.

For example, suppose that 60,000 shares of £1 each are offered for subscription, the issue being underwritten for a commission of 5 per cent. and an over-riding commission of 1 per cent. by Jones and Thompson, each guaranteeing 30,000 shares. Of Jones's underwriting Smith and Robinson sub-underwrite respectively 5,000 and 10,000 shares, and of Thompson's responsibility Wilson sub-underwrites 4,000 and Davis 6,000 shares.

The over-riding commission is intended to cover the remuneration of the underwriters for obtaining sub-underwriting, and subject to any agreement that the guarantors enter into as between

themselves, the ordinary disposition of the commission may be taken as under—

		Shares.
Jones's underwriters		30,000
of which are sub-underwritten		
by Smith	5,000	
Robinson	10,000	
		<u>15,000</u>
		<u>15,000</u>
Jones and his group would be entitled to the following sums—		
<i>Jones</i>	5 % on 15,000	£ 750
	1 % therein	150
	1 % on 5,000	50
	1 % „ 10,000	100
		<u>1,050</u>
<i>Smith</i>	5 % „ 5,000	250
<i>Robinson</i>	5 % „ 10,000	500
Total A and group		<u>£1,800</u>

		Shares.
Thompson underwrites		30,000
of which are sub-underwritten		
by Wilson	4,000	
Davis	6,000	
		<u>10,000</u>
		<u>£20,000</u>

Thompson and his group would be entitled to the following sums—

<i>Thompson</i>	5 % on 20,000	£ 1,000
	1 % thereon	200
	1 % on 4,000	40
	1 % „ 6,000	60
		<u>1,300</u>
<i>Wilson</i>	5 % „ 4,000	200
<i>Davis</i>	5 % „ 6,000	300
		<u>£1,800</u>

Jones and others	£ 1,800
Thompson and others	1,800
	<u>£3,600</u>

which equals 6% in £60,000

The following sets forth one of the several modes used in practice in ascertaining the liability of underwriters when they are "saddled." Sometimes the exact method of computing the liability is fully indicated in the agreement, and at others it is not infrequently vague from the accountant's point of view.

Let us assume that an issue of 60,000 shares is

underwritten, that the public subscribe for 36,000 of the shares, and that the following represents the liability of each underwriter and the shares "taken firm."

	No. of Shares underwritten.	Shares taken firm.
Jones	10,000	5,000
Smith	5,000	1,000
Thompson	2,500	2,500
Wilson	6,000	3,000
Davis	3,500	1,000
Robinson	30,000	5,000
Black	1,000	400
White	2,000	600
	<u>60,000</u>	<u>18,500</u>
Issue	60,000	100%
Public Subscribe	36,000	60%
No. of shares for which the underwriters are liable	<u>24,000</u>	<u>40%</u>

Dissecting the underwriting contracts we ascertain that—

Jones has taken firm	50% of his underwriting
Smith	20% " "
Thompson	" " all his underwriting
Wilson	" " 50% of his underwriting
Davis	" " 28·57% " "
Robinson	" " 16·66% " "
Black	" " 40% " "
White	" " 30% " "

Those who have taken 40 per cent. and over of their underwriting are Jones, Thompson, Wilson, Black, and the position at this stage is—

Public take	36,000
Jones	5,000
Thompson	2,500
Wilson	3,000
Black	400
	<u>10,900</u>
	46,900

leaving to be apportioned between Smith, Davis, Robinson, and White—

	13,100
Total issue	<u>60,000</u>

The apportionment may be made as under—

Smith	5,000
Davis	3,500
Robinson	30,000
White	2,000
	<u>40,500</u>
of which 13,100 shares represents 32·3456%.	

Smith takes 32·3456% of	5,000 = say	1,617
Davis	3,500 = "	1,132
Robinson	30,000 = "	9,704
White	2,000 = "	647
		<hr/> 13,100

The position finally is therefore as under—

Public		36,000
Jones	5,000	
Thompson	2,500	
Wilson	3,000	
Black	400	
		<hr/> 10,900
		46,900
Smith	1,617	
Davis	1,132	
Robinson	9,704	
White	647	
		<hr/> 13,100
		<hr/> 60,000

It is usually stipulated in underwriting agreements that the commission is not payable until the amount due on allotment has been paid.

The commission may be payable in shares as fully paid taking them at a certain premium when so quoted. For instance, a 6 per cent. commission on an underwriting of 3,000 shares of £1 each at a premium of 5s. per share.

6% on 3,000 = 180
and £180 = 144 shares to be allotted.
25/-

UNDISCHARGED BANKRUPT.

(See BANKRUPTCY ; UNDISCHARGED BANKRUPT.)

UNDISTRIBUTED PROFITS.

(See ACCOUNTS, CRITICISM OF.)

UNDUE PREFERENCE.

This term is used in two distinct senses. In the first place it refers to anything which is done by a railway or canal company which places different traders in different positions so far as the rates charged by the company are concerned. If anything of this kind takes place, the party or parties aggrieved have always a right of complaint to the Railway and Canal Commission, a judicial body appointed under certain statutes relating to railway and canal rates.

But the more general use of the term is in connection with bankruptcy proceedings, and the meaning that is then attached to it is some act or acts on the part of the bankrupt by which he has shown gross favoritism to certain particular creditors in paying their claims in full within the three months prior to the making of the receiving

order, by which his assets have been heavily diminished and the remainder of the creditors deprived of the whole or a part of the dividend which they would otherwise have received. It is obvious that undue preference must be a question of fact in every case, and must depend upon the special circumstances under which the preferential payment is made. Not only may the creditors who have been unduly preferred be made to disgorge in certain cases, but undue preference is a ground for the refusal or the lengthy suspension of a bankrupt's discharge.

UNEMPLOYMENT INSURANCE.

(See HEALTH AND UNEMPLOYMENT INSURANCE DEDUCTIONS.)

UNEXPIRED EXPENSES.

(See ADJUSTMENTS AT BALANCING TIME.)

UNEXPIRED PROPORTION OF PAYMENTS.

(See BALANCE SHEET, p. 153.)

UNIVERSAL AGENT.

This is an agent whose powers are practically unlimited in connection with his agency. He is, in reality, a person who is entitled to do everything which the principal could do on his own account. It is a very rare thing for a universal agent to be met with in commercial transactions. (See also AGENT.)

UNLIQUIDATED DAMAGES.

In all cases where there is a breach of an obligation, whether arising out of contract or tort, and the amount of the damages is not fixed or ascertained by some statutory provision, or by agreement between the parties, the damages are said to be unliquidated and can only be ascertained by a legal tribunal—either a judge sitting alone, or a jury. Thus, if a person sues for damages for non-delivery of goods, provided he proves his case, the damages to be awarded him are such a sum as represents the loss he has sustained by reason of the non-delivery. The amount is not fixed or liquidated, but has to be ascertained after inquiry. But the question of unliquidated damages arises most frequently in cases of tort, where one person has sustained some injury and a jury is called upon to assess what amount should be paid to him in respect of the same. (See LIQUIDATED DAMAGES.)

UNPAID DIVIDENDS ON PREFERENCE SHARES.

(See AUDITING, p. 90.)

UNSECURED CREDITORS.

(See BALANCE SHEET, p. 136; LIQUIDATORS, ACCOUNTS OF, p. 655.)

USANCE.

This is the time which is allowed by usage for the currency of bills of exchange drawn by one country upon another. Bills are sometimes drawn at one, two, or more usances.

USURY.

This is the name which formerly meant interest and is now generally applied to an exorbitant rate of interest charged for money lent. In olden times the law was exceedingly severe against persons who lent money at excessive

rates of interest, but the whole of the statutes concerning usury were abolished in 1854. Owing to the abuse of money-lending in recent years, two Acts have been passed, called the Money Lenders Acts, in 1900 and 1911 respectively. In addition to providing elaborate machinery as to the method in which money-lenders must now carry on their business, a borrower may appeal to the Court whenever there is an allegation that the bargain entered into with a money-lender is of a harsh and unconscionable character, and if the Court is satisfied that under all the circumstances the transaction is of a kind against which relief should be given, it will decree what is a fair and reasonable amount to be paid by the borrower to the lender in satisfaction of the latter's claim.

VALUABLE CONSIDERATION.

(SEE CONSIDERATION.)

VALUATION.

The method of ascertaining the value or price of anything, or the assessing of property for the purposes of taxation. (See QUINQUENNIAL VALUATION.) Valuations are provided for in many cases. Thus, it is a common term in articles of partnership for provision to be made that there shall be a valuation made upon the dissolution of the partnership in order to ascertain the share of the partnership property to which each partner is entitled. In bankruptcy, a secured creditor is entitled to value his security instead of realising the same, and then to prove for the deficiency (if any) in the bankruptcy proceedings. And, again, under the Lands Clauses Act, 1845, the purchase price of lands taken compulsorily by public bodies is in most cases ascertained by valuation.

VALUATION OF ASSETS.

(SEE ASSETS, VALUATION OF.)

VALUATION OF GOODWILL.

(SEE GOODWILL.)

VALUATION OF WORK IN PROGRESS.

(SEE WORK IN PROGRESS.)

VERIFICATION OF BOOK DEBTS.

(SEE BOOK DEBTS, VERIFICATION OF.)

VERIFICATION OF INVESTMENTS.

(SEE AUDITING, p. 97; INVESTMENTS, VERIFICATION OF.)

VERIFICATION OF STOCK.

(SEE STOCK, VERIFICATION OF.)

VESTED AND CONTINGENT GIFTS.

(SEE LEGACIES.)

VESTED ESTATE.

An estate which, whether in possession or not at the moment, must become the property of a certain person at some time or other if he lives long enough, and of which he can dispose as far as his interest is concerned. Naturally, the holder of an estate for the time being has a vested estate, but any other person who is to hold in succession to the present holder, provided his right to hold does not depend upon any contingency other than the termination of the interest of his predecessor, has also a vested estate, known generally as a

vested remainder. A good illustration of the difference between a vested and a contingent interest is shown by the bequest of a legacy. If a legacy is given to be paid *when* the legatee is 25 years of age, the right of the legatee is vested; he is entitled absolutely; and if he dies before 25, the legacy must be paid to his personal representative in any case, always providing the legacy has not lapsed by the legatee predeceasing the testator. If, on the other hand, the legacy is payable if the legatee attains the age of 25, this is contingent, and *if* the legatee does not in fact live to the age of 25, the legacy fails altogether and falls into the residue of the testator's estate.

VOID AND VOIDABLE.

These two words are sometimes met with in respect to contracts, and are contrasted as follows: A contract is void when it is destitute of all legal effect whatever, that is, when it cannot be enforced by any of the parties to it; whilst a contract is voidable if it is capable of being affirmed or repudiated by one or other of the parties according to his or their wishes. An example of a void contract is where the whole subject-matter is illegal and cannot be carried out at all; an example of a voidable contract is where an agreement has been entered into under duress, fraud, or misrepresentation, in which case the party injured has the right to repudiate or affirm at his option.

VOLUNTARY ASSOCIATIONS, AUDITORS AND.

(SEE AUDITING, p. 118.)

VOLUNTARY LIQUIDATION.

(SEE LIQUIDATORS, ACCOUNTS OF, pp. 644 and 665.)

VOLUNTARY SETTLEMENT.

A settlement is any conveyance, assignment, or transfer of property under which the transferor purports to part with his interest in the same in favour of the transferee. Such a settlement is voluntary when it is made for a consideration which is not held to be "valuable" in law. A settlement made *bonâ fide* and for valuable consideration is valid, if made before bankruptcy proceedings have commenced; but when there is not a valuable consideration, although the settlement is valid and subsisting as between the transferor and the transferee, it is void under certain conditions. If this were not so, a person on the eve of bankruptcy would divest himself of all his belongings and defraud his creditors entirely. In

order to set aside a settlement made within two years of the bankruptcy, it must be shown that the same was made in bad faith and without consideration. A settlement made within ten years will be set aside unless the parties claiming under it can prove that the settlor was able to pay his debts at the date of the execution of the settlement without the aid of the property comprised in it, and that the interest of the settlor passed to the trustees of the settlement under the settlement. Of course, if the settlement is void, the property passes to the trustee in bankruptcy for the benefit of the creditors. Marriage is a valuable consideration, and if a settlement is made before, and in consideration of marriage—that is, if it is an ante-nuptial settlement—that holds good against the trustee in bankruptcy, unless the whole transaction is tainted with fraud. But now, by the Bankruptcy Act, 1914, if a marriage settlement is entered into for the future payment of money for the benefit of wife, husband, or children, this is void if the settlor is adjudged bankrupt and the covenant or contract has not been executed at the date of the commencement of the bankruptcy, except in so far as it enables the persons entitled under the covenant or contract to claim for dividend on the settlor's bankruptcy under or in respect of the covenant or contract, but the claim to dividend is postponed.

VOUCHER.

A document vouching or certifying a certain transaction, especially a writing attesting the payment of money (e.g. a receipt).

VOUCHERS.

(See AUDITING, p. 74.)

VOUCHERS AND VOUCHING.

Any book or document which serves satisfactorily to evidence, authenticate, or confirm the correctness or otherwise of accounts, or to establish facts, may be described as a voucher, and vouching may be said to consist of the examination of entries in books, or book records in conjunction with the vouchers and other similar evidence relative thereto. Various definitions have been given from time to time of a voucher, and though expressed in varying terms the interpretation is not dissimilar. For instance, a voucher is evidence of payment which at the same time tests the accuracy of the payment, a receipt for cash paid and received, which is, of course, restricted. In its widest sense a voucher as we have indicated, means documentary evidence which satisfactorily evidences the existence of liabilities and assets and their correctness. The more direct and independent the instrument of evidence the greater its value. To verify means to prove or show to be true, and verification is the act or procedure of confirming, authenticating, or proving to be true.

TRAFFIC RECEIPTS OF A TRAMWAY COMPANY.—For example, to verify that all the traffic receipts of a Tramway Company have been accounted for, we may take the amount of receipts on the *Dr.* side of the Cash Book. The balance of takings completing the year not paid into the bank until the subsequent year, will have been vouched with the Bank Pass Book, and the traffic reports; examine the reports with the Traffic Book records, and the latter with the actual way bills. The ticket stock at the close of business on the last day of the financial year is taken, and extraction of the values of the tickets used, or issued as per the Ticket Stock Book may be made with the object indicated in view. We may now proceed to indicate and comment upon the evidence that is customarily available of cash receipts and payments and other transactions of similar effect.

RECEIPTS OF CASH IN PAYMENT OF SALES.

—With regard to the receipts of cash in payment of sales, or the items on the debtor side of the Cash Book, we may find in vogue receipt books of which the counterfoils are deemed to constitute a means of check, the effectiveness of which, however, is subject to internal procedure, and generally they may be regarded as *prima facie* evidence only. The most effective way perhaps is, after accounting for the whole of the sales, and the cash received, discounts allowed, and bills, to send to each outstanding customer a statement showing the amount on balance at the date of the accounts, and to state that it will be taken as being agreed or correct unless otherwise notified by a certain date. Such a course, however, in most cases is quite unnecessary, and in some circumstances it may be at least objectionable. On the other hand, it is very desirable in cases where it is the custom for travellers to settle accounts, that they should be provided with books of forms of official receipts, and for monthly or other periodic statements of accounts to be rendered by the office showing the position of the accounts at the date of rendering, with a request that immediate communication be made if unable to agree.

BANK INTEREST.—Bank interest—received and paid—will be vouched with the Bank Pass Book, and transfer fees with the number of transfers passed as per Transfer Register and Board Minutes. Transfers to and from deposit will be confirmed by the Bank Pass Book, which will also evidence all receipts paid into and all payments out of the bank account, the bank certificate at the date of the balance sheet vouching the precise position of the account at the bank, which, subject to the cheques outstanding, will be reconciled with the balance as shown by the Cash Book in the orthodox manner.

PURCHASE AND SALE OF INVESTMENTS.

—For the purchase and sale of investments there are

the brokers' sold and bought contract notes, and such receipts, letters, or acknowledgments as are common to all cases.

AUCTIONS.—Proceeds of auction sales and expenses in connection therewith in a liquidation (winding up by the Court) and in bankruptcy will be vouched by the allocation (it is allowed) or certificate by the taxing master of allowance of costs.

DIVIDEND.—For dividends (interim and final) and interest on investments the production of the usual printed letter to which the interest and dividend warrants are attached will be forthcoming, and as regards rents received we may notice *inter alia* the accounts rendered.

BUILDING SOCIETIES.—In the case of Building Societies whose profit primarily consists of the difference between interest charged to borrowers and interest paid to investors, it is required that every auditor in attesting the annual account or statement shall either certify that it is correct, duly vouched, and in accordance with law, or specially report to the society in what respect he finds it incorrect, unvouched or not in accordance with law, and also certify that he has at the audit actually inspected the mortgage deeds and other securities belonging to the society, stating the number of properties with respect to which the deeds have been produced to and actually inspected by him. It is of the utmost importance, of course, that all entries as well as additions and postings be carefully checked and all necessary vouchers produced, that all deposits received and deposits uplifted with interest thereon, sums received on account of the redemption of mortgages, or borrowers' shares or advances, income from properties in hand, subscriptions from unadvanced or investment on subscription shareholders, advances to borrowers, and withdrawals should be strictly verified, and that the transactions are in order; that is, in accordance with law, and the rules of the society, all pass books being carefully compared with the corresponding ledger accounts. The auditor will note the rules as to examination of pass books, investments of surplus funds, and the terms on which members may withdraw, and in particular the proportion of the total amount received on deposit or loan and not repaid by the society to the amount for the time being secured to the society by mortgages from its members.

SAVINGS BANKS.—The accounts of a savings bank in certain respects should be similarly examined and checked. In the case of gas and water companies, tramway and electric lighting companies, and telephone companies, all cash received and receivable must, of course, be accounted for.

ISSUE OF SHARES.—With regard to the amounts received on the issue of shares and debentures, these are, of course, checked with the

forms of application and call, sent with the remittances to the bank, and with the entries in the share or debenture pass books.

CASH BOOK.—As to the vouching of the items on the credit side of the cash book, all payments out of the bank should be checked with the entries in the bank pass book. The receipts of the payees may consist of official forms of receipt, receipted invoices, receipted dockets, letters, acknowledgments, or other similar documents. In company practice all payments are authorised or confirmed by the Board, particulars of which will be found either in the Minute Book or in the cheque Agenda Book. The kind of docket to which we refer may take the following form—

(Form to be returned entire)-----19--

M & N Co., Ltd.

To-----Dr.

Date.	Particulars.	Amount.	Total.

Acct.

-----19--
Received the sum of -----

as per details above

£-----

In those instances (and they are of frequent occurrence) in which payees have omitted to furnish receipts, the cheques will be available; but as evidence they are generally only of secondary importance or value. Many firms and companies have attached to their cheques a form of receipt, which must be completed (and stamped, if necessary) before they will be honoured by the bank on which they are drawn.

Transfers from current account at the bank to dividend and debenture interest accounts will be vouched with the bank pass books, and with the minutes for authority. Payments out of the dividend and debenture interest accounts will be vouched with the paid warrants and with the dividend or interest pass book.

Appropriations of dividends to the payment of outstanding calls, or calls in arrear, will be vouched with the particular dividends payable, the appropriation being usually effected by debiting sundry shareholders and crediting bank dividend account in the books of the company with the amount

appropriated. The transfer is recorded by the bank in the dividend and call pass books, and an entry is made on the *Dr.* side of the company's cash book which is posted to the credit of the call account.

For bills of exchange paid, the bills themselves will be produced, and the originals of renewed bills also will be submitted. In support of the payments of wages the auditor will or should have access to adequately certified wages sheets or pay bills.

PETTY CASH.—With reference to petty cash, the common practice is to draw cheques from time to time as petty cash is required upon the current account, such cheques, of course, being included among those sanctioned by the Board. The transfers will be, therefore, evidenced by the entries in the pass book. Vouchers will be at hand, at

any rate for the more important items of payment thereout. Where it is necessary to have in hand a large sum for petty cash or other purposes, it is well to count the cash on a given date, to vouch the payments since the date of closing the accounts to the date of verification of the existence of the petty cash balance, reconciling the balances at the two dates.

- For payments of rents, rates and taxes, and insurance, the usual descriptions of receipt will be produced—the voucher for the payment of a premium under a policy being usually the policy itself.

Partners should be required to give receipts for all their drawings. For payments under agreements, the receipts will be seen, and reference may be made to the agreements themselves. (See also INVESTIGATIONS, p. 575.)

VOYAGE No. 8

Newcastle—Buenos Ayres.
Buenos Ayres—London
—Newcastle.

S.S. "LONDON ABBEY."

To DISBURSEMENTS AT NEWCASTLE—				£	s.	d.	By Freights Earned—				£	s.	d.
Bunker Coals (per Engineer's Receipts).				325	0	0	OUTWARD: Coal, Newcastle to Buenos Ayres: 5,000 Tons of Coal at 11s. per ton						
Provisions, Stores, and Chandlery ..				248	0	0					2,750	0	0
Port Charges, Light Dues and Pilotage ..				95	0	0	HOMEWARD: Buenos Ayres to London, General Cargo (as per Manifests) ..				1,140	0	0
Captain's Account, for Wages, Harbour Dues, and various				183	0	0							
„ DISBURSEMENTS AT BUENOS AYRES—							Buenos Ayres to Newcastle, General Cargo (as per Manifests)				1,460	0	0
Inward Discharging Cargo: Stevedore				73	0	0							
Port Charges, Light Dues and Pilotage				213	0	0	PASSENGERS HOMEWARD: Buenos Ayres to London, 7 at £21 each				147	0	0
Captain's % for Wages advanced				182	0	0							
Agency Disbursements and Charges				63	0	0							
Outward Port Charges, Light Dues and Pilotage				136	0	0							
Provisions and Stores				314	0	0							
Coals				241	0	0							
Agency Charges				38	0	0							
„ DISBURSEMENTS AT LONDON—													
Port of London Charges, Pilotage, Light and Dock Dues				272	0	0							
Discharging Cargo				72	0	0							
Captain's Account for Wages Advanced				61	0	0							
Stores, etc.				22	0	0							
„ DISBURSEMENTS AT NEWCASTLE—													
Port Charges, Light Dues, and Pilotage ..				83	0	0							
Discharging Cargo				67	0	0							
Captain's Portage Bill				£812									
Less Advances on Voyage				£280									
Allotments to relatives of Seamen				£281									
— £561				251	0	0							
Captain's % for Expenses at Ports, etc. ..				42	0	0							
„ ALLOTMENTS MADE TO SEAMEN'S RELATIVES											443	0	0
CAPTAIN'S SALARY, 5 mos. at £20 per mon.											281	0	0
„ INSURANCE, Propn of Time Policy on Vessel											100	0	0
4½ months at £2,000 p. a.											750	0	0
„ INSURANCE ON FREIGHTS Outward ..				87	0	0							
Homeward				103	0	0					190	0	0
„ MANAGING OWNER'S COMMISSION—													
4% on Coal Freight. 4% on £2,750 ..				110	0	0							
5% on General Freight. 5% on £2,690 ..				131	0	0							
„ PROFIT ON VOYAGE											214	0	0
											951	0	0
											£5,497	0	0
											£5,497	0	0

VOUCHING BACK.

Checking the Ledgers by calling back from them to the books of original entry, so making the check the reverse way to that in which the original posting was done. (See also INVESTIGATIONS, p. 575.)

VOYAGE ACCOUNTS.

Irrespective of the pecuniary interest in the voyage, whether it be that of the owners or of charterers, it is usual in the case of ships to raise a separate account for each voyage of each ship. The voyages are numbered in sequence, and very frequently one book is kept for each ship, the account of each voyage following on the previous one in numerical order. A book with ordinary Cash Book rulings is sufficient for the purpose, the inner column being used for details and the outer column for totals. The particulars of receipts and payments are derived from several sources—

(1) From the accounts of the owners, charterers, or managers themselves.

(2) From the receipts and disbursements of the captain during the voyage, for he may collect freights at various ports and, in any case, has to make various disbursements (in many currencies).

(3) From the accounts furnished by the company's agents at those ports where the company has agents. The agents reimburse themselves for their outlays from the freights collected by them,

and account for the balance either to the captain or to the owners, as may be arranged.

Annual or other periodical payments should be apportioned according to the duration of the voyage.

If a vessel is chartered, the address commission payable to the charterers' agents should be charged against the Voyage Account, and if any proportion of the brokerage is repayable to the vessel, it is brought to the credit of the voyage. (A form of Voyage Account is shown on p. 934.)

The nature of the receipts and payments is given in the following illustration—

The s.s. *London Abbey*, 3,200 tons gross register, managed by Messrs. Church & Co., on behalf of the Abbey Steamship Co., Ltd., of Newcastle (owners of the Abbey Line), left Newcastle on 5th February, 19.., with 5,000 tons of coal for Buenos Ayres at 11s. per ton. Left Buenos Ayres with general cargo, freight, as per Manifests, being as follows: London Freight, £1,140; Newcastle Freight, £1,460; arriving at Newcastle 23rd June, 19...

The steamer was insured at Lloyd's at an annual inclusive premium of £2,000 per annum.

Seven passengers were carried to London on the homeward voyage at an inclusive rate of £21 each.

The Managing Owner's Commission is fixed at 4 per cent. on Gross Coal Freights, and 5 per cent. on General Freight.

WAGER.

It has been judiciously observed that, "The essence of gaming and wagering is that one party is to win and the other to lose upon a future event, which at the time of the contract is of an uncertain nature, that is to say, if the event turns out one way A will lose, but if it turns out the other way he will win." It is not illegal to make a wager; but all contracts by way of gaming or wagering are void under two Acts passed in 1845 and 1892 respectively. If a defendant wishes to rely upon these Acts, or either of them, as a defence in an action brought against him, there should be a special plea to this effect. Wagers are not confined to any one class of transactions. There may be wagering and gaming on the Stock Exchange as well as on a racecourse, and if it is proved that a wager has been made, the defence of the statutes is as complete in one case as in the other.

WAGES.

(See ADJUSTMENTS AT BALANCING TIME; INVESTIGATIONS, p. 586; MANUFACTURING WAGES; PROFIT AND LOSS ACCOUNT, p. 792; SALARIES AND WAGES; TRADING ACCOUNT, p. 918.)

WAGES BOOK.

A book kept for the record of employees and wages paid to them week by week, ruled to meet the requirements of the particular business in which it is employed. Thus, in an engineering business the number of hours each day, the weekly total, the rate per hour, and total due, are provided for, and in a retail establishment the weekly wage, any premiums due, and the total. Provision must also be made to meet the requirements of the National Insurance and Unemployment Acts.

WARRANTY.

A warranty is an agreement with reference to some thing or matter which has already been the subject of some contract or agreement between the parties concerned. It is, in fact, a superadded contract, for the breach of which an action for damages lies at the instance of the person damnified.

Although the question of warranty is not confined to personal property, but may arise in various cases upon the sale of real estate, the main incidents in connection with it are chiefly exemplified in the case of the sale of goods. By the Sale of Goods Act, 1893, a warranty is defined as "an agreement with reference to goods which

are the subject of a contract of sale, but collateral to the main purpose of such contract, the breach of which gives rise to a claim for damages, but not to a right to reject the goods, and treat the contract as repudiated."

The general rule as to contracts of sale of goods is that a person buys at his own risk, the maxim, *caveat emptor*, applying. But in the following cases a condition is implied—

(1) Where the buyer, expressly or by implication, makes known to the seller the particular purpose for which the goods are required, so as to show that the buyer relies on the seller's skill or judgment, and the goods are of a description which it is in the course of the seller's business to supply (whether he is the manufacturer or not), there is an implied condition that the goods shall be reasonably fit for such purpose, provided that in the case of a contract for the sale of a specified article under its patent or other trade name, there is no implied condition as to its fitness for any particular purpose.

(2) Where goods are bought by description from a seller who deals in goods of that description (whether he be the manufacturer or not), there is an implied condition that the goods shall be of merchantable quality; provided that if the buyer has examined the goods there shall be no implied condition as regards defects which such examination ought to have revealed.

(3) Where goods are bought by sample there is an implied condition that the bulk shall correspond with the sample, and shall be free from any defect rendering them unmerchantable, which would not be apparent on reasonable examination of the sample.

(4) An implied warranty or condition as to quality or fitness for a particular purpose may be annexed by the usage of trade.

An express warranty or condition does not negative a warranty or condition implied by the Sale of Goods Act, unless it is inconsistent with it. Any express warranty must be given at the time of the contract of sale, otherwise it must be supported by a fresh consideration.

Distinct from all questions of quality, there is an implied condition in every contract for the sale of goods (unless the contrary intention is shown) that the vendor has a right to sell the same, and that the goods are free from undisclosed encumbrances. A "contrary intention" would be shown if the vendor were a pawnbroker or a sheriff. Each can only transfer the right which

he has in the goods at the time of sale, and, in default of express warranty, is not liable for loss arising through a defective title.

In the case of marine insurance, also, there are special warranties implied, in addition to the express one usual in the policy of marine insurance. The principal of these implied warranties are sea-worthiness, non-deviation, and the legality of the voyage contemplated by the ship.

A warranty must be carefully distinguished from a condition (*q.v.*). The remedy for the person aggrieved by a breach of warranty is an action for damages. (See also SALE OF GOODS ACT, 1893.)

WASTE.

This is a legal term used in connection with real property, and indicates any alteration or change made in an estate by the tenant for life in possession. Waste is either voluntary or permissive. Voluntary waste consists in doing something to the property, for example, pulling down a house or altering it radically. (Even though the alteration may, in fact, render the property more valuable, it is still called waste, but generally "ameliorative waste.") Permissive waste consists in allowing the property to fall into decay. Without going into any details, it may be stated as a general proposition that a tenant for life is not liable for permissive waste, unless the duty to repair has been expressly laid upon him by the grantor of the estate. But he is liable for voluntary waste, unless the instrument of grant expressly declares that his estate is to be "without impeachment of waste." The remedy for waste by the remainderman is an action for damages or an injunction to restrain the waste. But even when a tenant for life holds his estate without impeachment for waste, the Court will restrain him from acts of wanton destruction or of a malicious character, such as the pulling down of the principal mansion-house of the estate. Waste of this last mentioned kind is generally styled "equitable waste."

WASTE BOOK.

A book in which particulars of every transaction of whatever nature is entered as it takes place. Waste Books are not now often kept by any but the smallest firms, although it is fairly common to find firms keeping rough Cash Books, which are practically Waste Books, for cash transactions.

WASTING ASSETS.

This term is applied to such assets as diminish in quantity or are consumed in the process of earning revenue, and which will not, in the nature of things, be renewed by the substitution of similar assets. Under this heading may be included quarries, mines, cemeteries, etc.

From a financial point of view, it is highly desirable that the loss of capital incurred in the consumption of these assets should be made good out of revenue. But, from a legal point of view, it is possible that dividends may be paid by a limited liability company out of the revenue arising from such assets without making any provision for the reduced values of the assets if the articles give power, although it will be necessary to make good any loss arising from circulating assets.

If this latter course is adopted by the companies dealing with wasting assets, the auditor should make it clear in his report to the shareholders that no provision has been made for the diminution of the capital values, so that the shareholders may, if they wish, make suitable provision for the maintenance of their own capital out of the dividends which are paid to them, since such dividends include a proportionate part of their capital. (See also DEPRECIATION, p. 394.)

WATER COMPANIES, BALANCE SHEET OF.

(See BALANCE SHEET, p. 149.)

WATERED CAPITAL.

Capital raised by a company by way of shares or stock in excess of what is warranted in view of the profits and prospects of the company, the effect of such issue being to reduce the rate of dividend, and, consequently, the market value of the shares or stock. This is usually accomplished by the inflation of values of assets, especially that of goodwill.

WAY-LEAVE.

A charge levied for drawing minerals through land belonging to proprietors other than the principal landlord, usually calculated at a rate per ton of mineral so drawn.

WIDOW'S RIGHT.

(See EXECUTORS AND ADMINISTRATORS.)

WILLS.

A Will is a written document in which a person sets out the way in which he wishes his property to be divided after his death. In order that legal effect can be given to such a document, it is necessary that it shall comply with the provisions of the Wills Act, 1837, and the amending Acts of 1861 and 1918.

Before the passing of the Wills Act, a variety of rules existed and, under these, wills by word of mouth, holograph wills, wills made by minors in respect of personalty were recognised. Under the Wills Act, however, writing is necessary in all

cases save in case of members of His Majesty's Forces on Active Service; signature and attestation of two witnesses are formalities now required, and minors, except soldiers and sailors, have no longer power to order the devolution of their property by will.

ESSENTIALS OF A VALID WILL.—Under the Wills Act, a will is required to be in writing, signed by the testator in the presence of two or more witnesses present at the same time. The actual signature may be made on behalf of the testator, and it should then be acknowledged by the testator in the presence of the witnesses. The signature of the testator appears at the foot or at the end of the will, that is, in such a position that it may be said to govern the whole of the writing. The witnesses must sign in the presence of each other and the testator, and in order to save trouble on the death of the testator, a statement known as an attestation clause should appear setting forth that the necessary formalities have been complied with.

The attestation clause takes the following form—

Signed by the said John Jones as his last will and testament in the presence of us both, being present at the same time, and who, at his request, in his presence and the presence of each other, have hereunto subscribed our names as witnesses.

(Signed) William Brown.

(Signed) Frank Robinson.

WILLS OF PERSONALTY.—The whole of the property at the testator's disposal will pass under his will made with the formalities above mentioned. The will is operative, even without an attestation clause, but difficulties arise when probate is required. Personal property differs from realty in many respects, the chief being that it is capable of moving and following the person of the owner. In consequence of that fact, the same considerations do not apply to personalty as to realty; and the Wills Act, 1861, provides that a will of personalty made by a British subject outside the United Kingdom is properly executed if it is—

(1) According to the law of the place where it is made; or

(2) According to the law of his domicile at the time he makes it; or

(3) According to the law of that part of the Dominions in which he had his domicile of origin.

Thus, a Scotsman, resident in Sweden, and formerly domiciled in the United States of America, may dispose of his personalty in England by means of a will according to Scottish law; according to Swedish law; or, if the will was made whilst he lived in the United States, according to the law of the States.

CODICILS.—Where a testator desires to make alterations or additions to his will, he may do so without affecting the main provisions by means

of a codicil. Such a document must be executed with all the formalities of a will (*i.e.* it must be signed by the testator and witnessed by at least two witnesses).

REVOCATION.—A will may be revoked either (i) by subsequent marriage of the testator; or (ii) by destruction of the document *with intent to revoke* either by the testator himself or by some other person in his presence and at his request; or (iii) by a later will or codicil formally executed and containing either an express intention to revoke or dealing with the property disposed of in a manner altogether inconsistent with the former will. Since a will speaks only from death, all property in the testator's hands at the time of his death and coming within the terms of the will passes under it, thus a gift of "all my real estate" passes property not in the hands of the testator at the date of the will but purchased before death. (See also EXECUTORSHIP ACCOUNTS, p. 447; INVESTIGATIONS, p. 589.)

WINDING UP.

(See LIQUIDATORS, ACCOUNTS OF.)

WITHOUT PREJUDICE.

When a difference has arisen between parties, either before or after litigation has commenced, there may exist a desire, on either side or on both sides, to effect a compromise and so avoid the anxiety and the expense of contesting the matter in dispute to the bitter end. It is open to either of the parties, either personally or through their legal advisers, to endeavour to arrive at an agreement, and provided it is clearly stated that all verbal communications are made without any admission of liability or as binding the parties, and that all letters which pass are marked "without prejudice," neither the verbal communications nor the contents of the letters can be made use of if the negotiations come to nothing and the case has eventually to be tried in Court. It is always understood that these communications, verbal or in writing, are made with a view to settlement, and that they do not on any account amount to an abandonment of a legal right. Neither the fact of such attempts at compromise nor the nature of the offers made can ever be made known to a judge or a jury. When letters are passing between the parties, it is not absolutely necessary that each of them should be marked "without prejudice." Any reply, or any one of a series of replies, to a letter which is marked "without prejudice" is bound to be kept back, even though not so marked, just as much as the first letter dispatched. It is always a question of tactics to what length this kind of communication or correspondence should be carried. It can easily be overdone, and a layman very frequently injures his case by marking a letter "without prejudice" when it

would be of great advantage to have the facts set out in the letter fully known to the Court.

WORK IN PROGRESS.

(See AUDITING, pp. 78 and 95; BALANCE SHEET, p. 152; COST ACCOUNTS, p. 356.)

WORKING ACCOUNT.

The Trading Account of a business whose gross profit is derived from working a natural product (e.g. quarrying, coal-mining, etc.). The account is debited with all expenses of conducting operations, and credited with the sales, the balance being the gross profit.

WORKING CAPITAL.

The capital introduced into a business, less the amount locked up in fixed assets, and the permanent amount of book debts and stock-in-trade, plus permanent loans and the permanent amount owing to creditors, that is, the amount which is available for conducting its operations and which is continually circulating. The working capital thus fluctuates considerably in amount, and the amount under control requires to be carefully watched. Losses arising through heavy expense should be avoided, and constant supervision kept over stock and book debts. Otherwise, unless the trader is in a strong position in regard to the amount of cash in the business, failure may accrue. This is often the case in over-trading, where, by the very success of the business, the working capital is depleted by being locked up in these directions.

As an example of working capital, consider the following—

Realisable value of debtors . . .	£	6,000
Bills Receivable negotiable . . .		4,000
Investments free and marketable . . .		3,000
Cash		5,000
Available liquid assets . . .		18,000
<i>Deduct—</i>	£	
Sundry Creditors		2,000
Bills Payable		2,000
Debenture Interest payable . . .		1,500
		<u>5,500</u>
Estimated working capital . . .	£	<u>12,500</u>

Other items may enter into the compilation of the statement, according to the nature of the business and the precise current circumstances.

In settling or arriving at the amount of capital required for the flotation and working of a company we may indicate the following outline by way of example; but, as just indicated, the statement is governed by the nature and magnitude of the proposed undertaking and other factors—

Purchase of Estates	£	80,000
Plant and Machinery		45,000
Stock-in-trade		10,000

135,000

to be satisfied by the allotment of 120,000 shares of £1 each in the Co. as fully paid and as to £15,000 in cash 135,000

Formation Expenses, Underwriting Commissions to the Capital expenses, say 2,000

Estimated working Capital required to bring the Estates to the revenue and profit-earning stage, including office and general expenses 40,000

It is proposed that the authorised capital of the company should be £250,000 in shares of the denomination of £1, and that 60,000 of the shares be offered to the public for subscription. We, therefore, have—

120,000 shares to be allotted as fully paid in part payment of purchase of Estates and other property;
60,000 shares to be offered for public subscription.

180,000

The estimated allocation of the £60,000 to be received from the issue of shares will be as under—

Formation Expenses will absorb . . .	£	2,000
Vendor's cash payment requires . . .		15,000
Leaving for working Capital purposes and Sundries		43,000
		<u>£60,000</u>

The real capital of a company, as distinguished from what may be termed its legal capital, may be expressed as under.

Fair valuation of fixed and floating assets less liabilities, such as creditors, bills payable, debentures and debenture interest, and other similar items, but excluding reserves.

Debentures, or debenture stock, do not form any part of the capital of a company. They are sometimes termed loan capital.

As another illustration, the X Y Z Co., Ltd., was formed for the purchase of certain properties, and the whole of the issued share capital, with the exception of the seven signatories' shares, was allotted as fully paid to the vendors, in satisfaction of the purchase of the properties, the latter being under obligation to provide a certain amount of working capital as to so much at once, and the balance from the proceeds of the shares sold.

WORKS ONCOST.

(See COST ACCOUNTS.)

WRIT.

In its broadest sense a writ is the King's precept in writing under seal issuing out of some Court, and commanding something to be done. In its more ordinary sense, a writ, also called a writ of summons, is the name given to the document by which an action at law is commenced in the High Court, the corresponding document issued out of a County Court being known as a plaint note or a default summons. This document is issued by or on behalf of a plaintiff, and commands the defendant, or the defendants, if there are more than one, to cause an appearance to be entered in the High Court within eight days. (In the country the District Registry takes the place of the High Court.) The writ is issued in the name of the Lord Chancellor; but if this office is vacant the Lord Chief Justice takes his place for the time being. The writ must be served upon the defendant in some such manner that it is either brought to his notice in fact, or presumed to have been brought to his notice in such way as the Court

shall deem sufficient. There are special rules as to service in particular cases, but these need no notice here. The general nature of the claim made by the plaintiff must be endorsed on the writ. Service should be effected within twelve months of its issue, but if this is impossible, a renewal may be obtained for six months, and at the end of the six months further renewals may be successively applied for on good cause being shown why service has not been effected. The object of these renewals is to prevent the Statutes of Limitations barring the right of action by reason of the lapse of time, for so long as the writ is in existence the Statute does not run. If a defendant does not enter an appearance to the writ within eight days, the plaintiff may sign judgment. If he does appear, the action takes its ordinary course.

Although one speaks of serving a writ, in practice it is a copy of the writ which is served upon the defendant, though the original must be produced for the defendant's inspection, if required. A writ may be served at any hour of the day or night except Sundays, Christmas Day, or Good Friday, though a trespass cannot be justified in the process of serving.

YEARLY TENANCY.

(SEE TENANCY FROM YEAR TO YEAR.)

APPENDIX

APPENDIX

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APPENDIX

[INC]

I

[INC]

INCOME TAX.

INTRODUCTION.—Income Tax, as its name implies, is a tax upon income, and was re-imposed in 1842, a somewhat similar tax having been originally introduced by Mr. Pitt in 1799, which, after being modified by the Income Tax Acts of 1803, 1805 and 1806, had been removed from the fiscal system of the country in 1816. As introduced in 1842, the tax affected Great Britain only, Ireland not being subjected to the charge until the Act of 1853 came into operation. From 1842 onwards numerous acts were passed, but in 1918 the whole were consolidated in the Income Tax Act of that year. This Act supersedes all the preceding Acts, so that the statute law relating to Income Tax is now found in the Income Tax Act of 1918, and the Acts passed subsequent to that date.

It is a direct tax, and is chargeable annually from the 6th April to the following 5th April, and is granted for one year only. In order, however, to ensure the collection in due time of tax which may be granted for any year commencing on the 6th April, all such provisions contained in this Act¹, or in any other Act relating to tax (including super-tax) as were in force on the preceding day, shall have full force and effect with respect to tax which may be so granted, in the same manner as if the said tax had been actually granted by Act of Parliament and the said provisions had been applied thereto by the Act. (Sec. 210.)

The persons who are liable to assessment under the Income Tax Acts are—

(a) All persons resident in the United Kingdom, whether subjects of His Majesty or not.

(b) All persons not resident within the United Kingdom (whether subjects of His Majesty or not) in so far as they derive income from property, trade, employment or vocation in the United Kingdom.

[NOTE. The term "person" under the Income Tax Acts includes bodies politic or corporate, or collegiate. Thus, a limited company is a person within the meaning of the Acts. But the term "individual" does not extend to limited companies, and exemptions or relief that are allowed to individuals cannot be taken advantage of by limited companies and other corporate or

incorporate bodies. An exception to this, however, occurs in the case of an unregistered Friendly Society, where exemption is allowed if the total income does not exceed £160.]

The principle adopted by the Inland Revenue authorities is as far as possible to tax at the source, thereby saving considerable time and expense in collection. Thus, Income Tax on property, with certain exceptions, is collected from the tenant, who is authorised by statute to deduct the whole or part from his next payment of rent to his landlord. Agents entrusted with the payment of income from Imperial, Colonial and Foreign public revenue are responsible to the Inland Revenue authorities for the tax upon all funds distributable by them, but are authorised to deduct the necessary amount before making payment. An exception occurs in the case of small dividends, and also in the case of certain loans issued during the war. Persons paying yearly interest, annuities or other annual payments are required to account to the authorities for Income Tax upon amounts payable, and have the right of deduction when paying to the recipient.

Companies are taxed upon their whole profits, the shareholders bearing their respective proportions of the tax by receiving so much less in dividends distributed. Partnerships stand in a more or less similar position to companies, their profits being assessable as a whole, although each partner can obtain, as can a shareholder of a company, any allowance, exemption, or repayment that he may be entitled to.

By the Finance Act of 1908 individuals in receipt of earned income were entitled to a special allowance where the income did not exceed a certain amount, but this was altered by the Finance Act, 1920, which provides that an allowance of one-tenth of the earned income shall be made, but that in no case must this allowance exceed £200.

EARNED INCOME.—The point of differentiation between income earned and unearned or investment income is important, and the statutory definition of the former may conveniently be given *in extenso*—

Income Tax Act, 1918, Section 14. Subsection (3). " . . . the expression earned income means—
"(a) any income arising in respect of any remuneration from any office or employment of

¹ The Act of 1918.

profit held by the individual, or in respect of any pension, superannuation, or other allowance, deferred pay, or compensation for loss of office given in respect of the past services of the individual, or of the husband or parent of the individual in any office or employment of profit, or given to the individual in respect of the past services of any deceased person, whether the individual or husband or parent of the individual shall have contributed to such pension, superannuation allowance, or deferred pay or not; and

"(b) any income from any property which is attached to or forms part of the emoluments of any office or employment of profit held by the individual; and

"(c) any income which is charged under Schedules B or D, or the rules applicable to Schedule D, and is immediately derived by the individual from the carrying on or exercise by him of his profession, trade, or vocation either as an individual, or, in the case of a partnership, as a partner personally acting therein."

Earned income, therefore, includes—

(a) Income from trades, professions, employments or vocations.

(b) Income from any public office or employments.

(c) Income from the occupation of land (*i.e.* farming profits).

(d) Income from property, the free occupation of which is part of the emoluments of the employment (*e.g.* a house occupied by a brewer without payment of rent, his employers being the owners).

(e) Pensions and the like received in respect of the past services of the taxpayer, her husband or parent.

INVESTMENT INCOME.—Investment income covers that which is received without exertion on the part of the recipient or not in consideration of past services above referred to, *viz.*—

(a) Income from property (including property occupied by taxpayer) other than exception already mentioned.

(b) Income from interest, annuities, dividends, etc., whether the dividends are from private or public limited companies.

(c) Income from a sleeping or limited partnership.

[NOTE.—Limited companies are not entitled to relief in respect of earned income.]

The income referred to in the Income Tax Acts, and assessable to the duties thereunder, is what is usually termed the statutory income, and does not necessarily correspond with the actual income of the taxpayer. This is a source of confusion to many people, but when it is considered that, before collection of tax in January of each year, returns have to be made by the public, and examined and inquired into by the assessors and

inspectors, that assessments have to be made and appeals as far as possible heard, it appears reasonable that the actual results of the year of assessment could not conveniently be dealt with.

It will be seen later that the income of lands, houses, etc., is often fixed quinquennially, and that, subject to certain rights of the owner with regard to appeal and repayment, the amount so determined is the income from such lands, etc., for the purposes of Income Tax. Considerable labour must be saved by adopting such a method as compared with one whereby the income of the year of the assessment is the basis of the charge. Businesses, professions, etc., are taxed on the average profits of a number of years prior to the year of assessment, which has the advantage of tending to keep the collections from Income Tax more regular from year to year, than would be the case if the profits were taxed on a basis of one year only.

ADMINISTRATION.—The officials through whom the Income Tax Acts are put into operation, and with whom the tax-paying public comes in contact, are the Assessor, the Inspector of Taxes, the Commissioners, the Clerk to the Commissioners, and the Collector. The following is a brief outline of their respective duties—

1. **The Assessor** prepares lists of all persons probably assessable to Income Tax under Schedule D, furnishes the public with the forms of return to be filled up within 21 days, records the amounts appearing on the returns, and estimates the assessable income where there is a failure to make a return.

2. **The Inspector of Taxes.** The returns and assessments are then examined by this official, who has power of amendment and surcharge before delivery to the Commissioners. He also sends out forms when no response has been made to the notices sent out by the Assessor. The tax-paying public comes largely in contact with the inspector, to whom notices of appeal are sent, and who conducts appeals before the Commissioners on behalf of the Inland Revenue. It is to him that accounts are furnished on appeal, and much trouble may be saved by agreeing with him an assessment which he will support before the Commissioners.

3. **The Commissioners** (District, General, Special and Additional). These are the chief officials who administer the Income Tax Acts, and are either District Commissioners (otherwise known as Commissioners for General Purposes) or Special Commissioners. Whilst the District Commissioners are distinct from the Board of Inland Revenue, being generally appointed from the Land Tax Commissioners, the Special Commissioners are Government officials. Additional Commissioners are appointed by the General

Commissioners, and generally are from their own number. All these officials deal with the assessments under the various Acts in their different spheres. The Additional Commissioners make the assessments after examination of the lists delivered to them, except in cases where the taxpayer elects to be assessed by the Special Commissioners, and either the General or Special Commissioners hear appeals therefrom. It is in the election of the taxpayer as to whom appeal is made, and the important point here arises, that there is no appeal from the decision of the General Commissioners upon a question of fact, whereas the Special Commissioners may be called upon to state a case to the Board of Inland Revenue on such a question. Questions of law in either type of appeals may be carried to the High Court for decision, and from there to the House of Lords. The duties of the Special Commissioners include the assessment of income to Super Tax, the assessment of incomes where the taxpayer elects that they shall assess, the assessment of railway companies under Schedule A, and of their officials under Schedule E, of certain income under Schedule C, and the hearing of appeals against assessments made by themselves, etc. In addition to these duties, they deal with all assessments in Ireland.

4. Clerk to the Commissioners. This official's duties are, *inter alia*, to attend the meetings of both the General and Additional Commissioners, to act as their adviser, to make abstracts of the returns of statements delivered to the Commissioners, to prepare duplicates of assessments, to make out the notices of assessment for delivery to the taxpayer, and to furnish him with particulars as to the hearing of appeals against them.

5. Collector. The Collector, who is usually the Assessor, makes demand for payment of tax in due course. In him is vested the right of distraint for duties in arrear.

CLASSIFICATION OF INCOME.—The different sources of income under the Income Tax Acts are classified under five schedules, viz., A, B, C, D and E, which may be conveniently explained as follows—

1. Schedule A deals with the income of owners of houses and land based upon rent or annual value.

2. Schedule B deals with the income of occupiers of land as regards the profits of such occupation, based, as in the case of Schedule A, upon rent or annual value, the duty, however, being charged upon twice the gross annual value, including tithe, subject to the right where the occupation is for the purpose of husbandry only (a) to be assessed on the actual profits of the year of assessment, if proved at the end of the year of assessment (see Income Tax Act, 1918, Schedule

B (6); and (b) to be assessed under Schedule D if within two months from the commencement of the year of assessment, the election to be so assessed is signified to the Inspector of Taxes for the District (see Income Tax Act, 1918, Schedule B (5)).

3. Schedule C covers the tax of income from Imperial, colonial and foreign public revenue, which is levied upon the amount received.

4. Schedule D, sub-divided into six cases (set out below), charges the profits of any trade, profession or other occupation not included in any other schedule.

CASES UNDER SCHEDULE D

Case 1 has reference to the profits of any trade, manufacture, adventure, or concern in the nature of a trade.

Case 2 covers the income from professions, employments or vocations not contained in any other schedule.

Case 3 embraces profits of an uncertain annual value not charged in Schedule A.

Case 4 deals with interest arising from colonial and foreign securities other than that to be charged under Schedule C.

Case 5 covers income from colonial and foreign possessions.

Case 6 treats with annual profits or gains not falling under any other schedule.

Income falling under cases 1, 2 and 5 is generally charged upon an average of three years, that under cases 3, 4 and 6 being generally upon one year's results.

5. Schedule E forms the charge for income of persons employed under the State, or otherwise publicly employed, such as officials of public corporations or companies.

Incomes not Chargeable. Certain income is not assessable to Income Tax, the chief instances being—

(a) Rents, dividends and other income devoted to charities, hospitals, etc. The buildings of almshouses, hospitals, etc., are also exempt in respect of tax under Schedule A.

(b) Similar to income under the previous heading, that of friendly, industrial and provident societies is exempted, and the universities and similar institutions, including the British museum, are not taxed in respect of public buildings belonging to them.

(c) Trade unions, approved societies under the National Insurance Act, and savings banks, all can claim relief from Income Tax.

Rates of Income Tax and Super-tax. The Finance Act, 1921, continues the standard rate of Income Tax at 6s. in the £, but it is provided that the first £225 of the taxable income of an individual (such taxable income being arrived at in accordance with the rules set out later) shall be charged at half the standard rate, namely, 3s.

in the £. In addition to this tax super-tax at the following rates is chargeable—

Part of Income Between	Rate.	Tax.	Cumulative.
	s. d.	£ s. d.	£ s. d.
£ 0 and £2,000	Nil	Nil	Nil
£2,001 „ £2,500	1 6	37 10 0	37 10 0
£2,501 „ £3,000	2 0	50 0 0	87 10 0
£3,001 „ £4,000	2 6	125 0 0	212 10 0
£4,001 „ £5,000	3 0	150 0 0	362 10 0
£5,001 „ £6,000	3 6	175 0 0	537 10 0
£6,001 „ £7,000	4 0	200 0 0	737 10 0
£7,001 „ £8,000	4 6	225 0 0	962 10 0
£8,001 „ £20,000	5 0	3,000 0 0	3,962 10 0
£20,001 „ £30,000	5 6	2,750 0 0	6,712 10 0
Over £30,000	6 0		

Assessment under Schedule A. Under this schedule, assessments are usually made quinquennially, and the different classes of income assessable thereunder are grouped under three headings—

No. 1 OF SCHEDULE A. The annual value of lands, tenements, hereditaments or heritages capable of actual occupation other than the properties mentioned under headings No. 2 and No. 3 referred to below.

This heading covers lands and buildings, which are assessed at the annual value thereof estimated as being the annual rents at which the same are let at rack-rent, if fixed by agreement within seven years before the time of making assessment, but, if not so let, then at the rack-rent at which the same are worth to be let by the year. The annual value thus arrived at is then reduced in accordance with Income Tax Act, 1918, Schedule A, v, 7, 8. The term “rack-rent” refers to the full letting value of the property to be assessed (*i.e.* the amount a landlord might reasonably expect to receive where he does repairs and the tenant pays the usual tenant's rates and taxes).

It will be seen that no difficulty is experienced where rack-rent is received, as that determines the annual value; but in other cases the value has to be arrived at by the Commissioners from such information as they have before them.

Where properties are let and the rent does not represent the whole consideration given, the value of the consideration other than rent is reduced to terms of annual value, and the resulting figure is then added to the amount of rent payable. Cases in point would be (a) a lump sum may have been paid in consideration of a lease being granted at a low rent; or (b) a low rent may be payable in respect of land in consideration of a building having been put up by the lessee, or of an existing building having been rebuilt. In both these instances, it is obvious that the rent payable could not be treated as the annual value, and that in case (a) the lump sum paid, and in case (b) the cost of the building, would have to be taken into account.

The Valuation (Metropolis) Act, 1869, now governs the assessment under Schedule A of lands and buildings in the metropolitan area, and the gross values of profits stated in the valuation list for Poor Rate purposes prepared under that Act are used as a guide in arriving at the annual value under the Income Tax Acts of properties in that district.

In the case of *Walker v. Brisley* (1900), Tax Cases, 254, it was held that the General Commissioners were not bound to adopt the gross annual value in the Poor Rate as the maximum annual value. The premises referred to were a fully-licensed public-house owned by the appellant company.

Repairs. Deduction for repairs from the gross value is allowed, and is provided for as follows—

(1) “Where tax is charged upon annual value estimated otherwise than by relation to profits, the following provisions shall have effect—

(a) In the case of an assessment on lands inclusive of the farmhouse and other buildings (if any), the amount of the assessment shall, for the purpose of collection, be reduced by a sum equal to one-eighth part thereof; and

(b) In the case of an assessment upon any house or building (except a farmhouse or building included with lands in assessment), the amount of the assessment shall, for the purpose of collection, be reduced—

(1) Where the owner is occupier or chargeable as landlord, or where a tenant is occupier and the landlord undertook to bear the cost of repairs, by a sum equal to one-sixth part of that amount; and

(2) Where a tenant is occupier and undertook to bear the cost of repairs, by such a sum not exceeding one-sixth part of that amount, as may be necessary to reduce it to the amount of rent payable by him.

(2) Where the amount of the assessment in the case of lands (inclusive of the farmhouse and other buildings) is more than one-eighth, and in the case of any house or building (except a farmhouse or building included with lands in assessment) is more than one-sixth, below the rent, after deducting from such rent any outgoings which should by law be deducted in making the assessment, this rule shall not apply.” Income Tax Act, Schedule A, v, 7.

It will be seen from this Section that the gross value is reducible in the case of lands (inclusive of farmhouses and other buildings (if any) by one-eighth part, and in the case of other houses or buildings by one-sixth part, but where the tenant of any such house or building undertakes to bear the cost of repairs the gross annual value must not be reduced by the full sixth part, if the effect be to reduce the Schedule A assessment to a sum less than the rent payable by him. Thus,

where house property is let at a rack-rent of £60, the *landlord* being liable to repairs, the assessment for Schedule A would be £50, arrived at as follows—

	£	s.	d.
Rents receivable for year	60	0	0
Less deduction one-sixth of £60	10	0	0
Schedule A assessment	£50	0	0

But where property is let at a rent of £60 and the *tenant* undertakes repairs, the assessment for Schedule A must not be less than this amount (in accordance with the rule quoted above). Although the gross annual value of this property may have been estimated as being £66, only £6 may be deducted in arriving at the assessment, as, if the full sixth of £66, viz., £11, were allowed, the assessment would be less than the rent. Were the full £11 deducted it will be seen that £5 of the landlord's income would escape taxation, which, from an Income Tax point of view, is undesirable.

The owner of any land (inclusive of farm-houses and other buildings (if any) or of any houses or buildings of an annual value of £12 or under as adopted for the purpose of Income Tax under Schedule A, is entitled, in addition to the relief allowed under the Section just referred to, to repayment of the amount of duty on the excess that the cost to him of maintenance, repairs, insurance and management, according to the average of the preceding five years, has exceeded the allowance made in arriving at the amount of assessment (see p. 986).

Rates. Where a landlord pays rates, inhabited house duty, and other similar expenses usually borne by the tenant, in arriving at the amount from which the one-eighth or one-sixth is deducted, a deduction of such expenses is made. Thus, where a property is let weekly to a tenant at an inclusive rent of 10s. per week, and parochial rates, water rate, and inhabited house duty are paid by the landlord annually, amounting in all to £6, the Schedule A assessment would be £16 13s. 4d. arrived at as follows—

	£	s.	d.
Rent receivable for year at 10s. per week	26	0	0
Deduct Rates (parochial and Water) and Inhabited House Duty	6	0	0
	20	0	0
Deduction—one-sixth of £20	3	6	8
Schedule A assessment	£16	13	4

Drainage and Embanking Rates, Embankments, Land Tax, Tithe Rent Charges. Expenses coming under any of these heads may be claimed as deductions in arriving at the Schedule A assessment, but in the case of tithe rent-charge, the amount so deducted is assessed separately on the person

owning the tithe after allowing therefrom deductions for costs of collection and rates paid thereon.

PERSONS ASSESSABLE

(a) *Tenant Assessable.* It has been mentioned above that, with certain exceptions, the occupier is assessed. This is in accordance with the principle of taxation at the source, and if such occupier is a tenant, he is entitled, under Rule (4) to No. VIII of Schedule A, to deduct from his next payment of rent an amount corresponding with the sum paid by him for Income Tax in respect of the property rented, but the sum so deducted must not exceed the amount of tax paid or a sum calculated at the rate for the time being upon the rent payable.

Thus, a tenant who is assessed at £60 when tax is 6s. in the £ and pays a rent of £50 can only deduct £15 from his next payment of rent; and a tenant who is assessed at £60 when Income Tax is at the 6s. rate and pays £70 as rent can deduct £18 from his rent, viz., 6s. in the £ on £60.

The landlord is bound to allow the deduction under a penalty of £50, but the tenant has no right to deduct other than from the next payment of rent (see *Cumming v. Bedfordborough* (1846) 15 M. and W. 438) except where such next payment is made *prior* to the passing of the Finance Act for the year, when he may deduct it from the next payment *after* the passing of the Act imposing the tax. (See Income Tax Act, 1918, Section 211 (2).)

Cases

(1) But under the particular circumstances, which obtained in *re Sturmeys Motors, Ltd., Rattray v. Sturmeys Motors, Ltd.* (1913), 107 L. T. 523, a receiver was held to be entitled to deduct payments of income tax from future payments of rent.

(2) The case of *Hancock & Co. v. Gillard* (1907) 95 L. T. 680, decided that compensation fund charge deducted by a licence holder under the Licensing Act, 1904, should be treated as being part of the rent paid, and that the tenant was entitled to deduct tax on the whole amount of rent.

(b) *Landlord Assessable.* The landlord is assessed instead of the occupier in the following cases—

(a) If the property is under the annual value of £10, or let for a period of less than one year.

(b) If the property is let in different apartments or tenements, and is occupied by two or more persons severally.

(c) If before the 31st July in the year of assessment the landlord requests to be assessed under Income Tax Act, 1918, Schedule A, vii, 9, and the General Commissioners are willing to assess him.

[NOTE. In each of these cases the authorities have the right of levying the charge upon the occupier, who may deduct it from *any* subsequent payment of rent.]

NO. 2 OF SCHEDULE A. The assessment of the following is upon the annual value based on the average amount of profits received—

(1) Tithes, if taken in kind, on an average of the three preceding years.

(2) Dues and money payments in right of the church or by endowment, or in lieu of tithes (not being tithes arising from lands) and of all teinds arising in Scotland, on an average of the three preceding years.

(3) All tithes arising from lands, if compounded for, and of all rents and other money payments in lieu of tithes arising from lands (except rent charges confirmed under the Act passed for the commutation of tithe) on the amount of such composition, rent, or payment for one year preceding, less a deduction for parochial rates.

[NOTE. A tithe rent-charge, as has been seen above, is deducted in arriving at the Schedule A assessment of a property on which it is charged, and under Income Tax Act, 1918, Schedule A, vii, 7, is chargeable on the tithe-owner. Rates paid are allowed as a deduction, as also are costs of collection. (*Stevens v. Bishop* (1888) 2 Tax Cases, 249.)]

(4) Manors and other royalties, including all dues and other services or other casual profits (not being rents or other annual payments reserved or charged) on an average of the seven preceding years to be charged on the lord of such manor or royalty, or person renting the same.

(5) All fines received in consideration of any demise of land or tenements (not being parcel of a manor or royalty demisable by the custom thereof) on the amount so received, within the year preceding by, or on account of, the party; provided that in case the party chargeable shall prove, to the satisfaction of the Commissioners for General Purposes in the district that such fines, or any part thereof, have been applied as productive capital, on which a profit has arisen or will arise otherwise chargeable under the Income Tax Acts, for the year in which the assessment shall be made, it shall be lawful for the said Commissioners to discharge the amount so applied from the profits liable to assessment under this rule.

[NOTE. The words "that such fines, or any part thereof, have been applied as productive capital" do not cover the case where fines received have been placed on deposit at a bank at interest. In the case of *Mostyn v. London* (1895) 3 Tax Cases, 294, the appellant was held to be assessable on the amount of fines so deposited.]

(6) All other profits arising from lands, tenements, hereditaments, or heritages, not in the actual possession or occupation of the party to be charged, and not before enumerated, on a fair and just average of such number of years as the said Commissioners shall, on the statement of the party to be charged, judge proper, to be charged on the

receivers of such profits, or the persons entitled thereto.

NO. 3 OF SCHEDULE A. The assessment of the following is upon the annual value based on the average amount of profits received—

(1) Quarries of stone, slate, limestone or chalk in the United Kingdom on the amount of the preceding year.

(2) Mines (other than alum mines) in the United Kingdom, on the average of the five preceding years. Where a mine is failing from some unavoidable cause, so that an assessment upon a five-year average would operate unfairly on the taxpayer, relief may be obtained on application to the General Commissioners, and in the case of a mine having totally failed, a discharge of the assessment may be obtained.

(3) Ironworks, gasworks, salt springs or works, alum mines or works, waterworks, streams of water, canals, inland navigations, docks, drains, and levels, fishing, rights of markets and fairs, tolls, railways and other ways, bridges, ferries, and other concerns of the like nature, from or arising out of any lands, tenements, hereditaments or heritages in the United Kingdom on the profits of the year preceding.

Under Income Tax Act, 1918, Schedule A, iii, 8, concerns falling under No. 1, 2, 3 (above) are assessable in accordance with the rules to be followed in assessing under Schedule D, except that railways have to be assessed by the Special Commissioners. It should be remarked that this does not alter the period on which the average has to be calculated, but makes the Schedule D rules applicable in their reference to deductions, procedure, etc.

Assessment under Schedule B. It has been seen that the assessment under this schedule is made upon the profits of occupation of land, and, therefore, the charge is in addition to Income Tax paid under Schedule A. Income under Schedule B differs from that assessable under Schedule A in being "earned" income. The occupiers of farms with their buildings, hop grounds, nurseries and market gardens come under this schedule.

The assessment is based upon twice the gross annual value of the land inclusive of tithe, except as regards nurseries and market gardens, which are directed to be assessed according to the rules of Schedule D.

The profits arising from the occupation of lands occupied by a dealer in cattle or milk, are assessable under Schedule B, unless the Commissioners find that the lands are not sufficient for the keep and sustenance of the cattle brought on the said lands, so that the rent or annual value cannot afford a just estimate of the profits of such dealer. On such a finding the Commissioners may call for a return of profits and charge him such further

sum as shall make up the amount which the trader would have had to pay if charged in accordance with rules of Schedule D.

Concessions are allowed to the farmer who occupies a farm for the purpose of husbandry only. These are granted under Income Tax Act, 1918, Schedule B, 5 and 6. Under the latter rule, if he shows at the end of any year to the satisfaction of the General Commissioners, that his profits and gains arising from the occupation of his farm, fell short of twice the annual value on which he had been charged, he can claim repayment of tax on such amount as he may have been assessed over and above the actual amount of his profits.

Rule 5 allows a farmer to elect to be assessed under Schedule D, but notice has to be given to the Inspector of Taxes within two months after the commencement of the year of assessment of his election to be so assessed. The effect of this election would be to have the average of the profits of the three years prior to the year of assessment assessed, instead of twice the gross annual value, inclusive of tithe. A farmer should arrange to be assessed under the schedule under which least tax is payable.

Assessment under Schedule C. Assessment under this schedule is upon "Annuities, dividends and shares of annuities" payable out of public revenue, whether Imperial, colonial or foreign, with certain exceptions. It is made upon the person entrusted with the payment of the revenue, if resident in the United Kingdom, and is assessed on the actual receipts of the year of assessment. As a set-off against the assessment being made on the distributing agent, he is empowered to retain out of the annuities, etc., such sum as he has to pay as tax upon assessment under this schedule. The recipients are required to allow the deduction made from the amounts to which they are entitled.

The exceptions referred to above, as not being assessable under Schedule C, are—

(a) Small annuities, dividends, etc., where the half-yearly payment does not exceed 50s. and is not paid by way of coupons on bearer securities.

(b) Stocks of friendly societies, savings banks, charitable institutions, registered industrial and provident societies, trade unions, etc.

[NOTE. The recipients of amounts received without deduction of tax are required to return them for assessment under Schedule D.]

REPAYMENT. If a person is not resident in the United Kingdom, and owns securities of a Foreign State or British Possession, the dividends of which are payable in the United Kingdom, he is entitled to reclaim at any time within three years of the end of the year of assessment, any tax that has been deducted at the time of receipt by him. If such securities are held in trust, the owner is deemed to be the person who is the beneficiary in

possession and can at any time effectively call upon the trustees to transfer the securities to him absolutely free from any trust.

Assessment under Schedule D. With a view to the proper assessment of income chargeable under this schedule, the person assessable has to make a return of such income in the required form, whether he has received notice to do so or not. Refusal, or neglect to do so, or the making of an incorrect return, lays the taxpayer open to penalties not exceeding £20 and treble the duty chargeable if the proceedings are before the Commissioners, or £50 if the proceedings are in the High Court and treble duty has not been charged. If a person to whom notice to make a return has been sent has no income chargeable, he must still make a return to that effect under a penalty not exceeding £5 for failing to do so.

The person making the return may elect to be assessed by the General or Special Commissioners, and may be assessed by letter or number. If no election is made, the General Commissioners will assess. The object of giving the right to be assessed by the Special Commissioners is to meet the case of an individual who prefers that his financial affairs should not come before the General Commissioners, who may be competitors in business.

In due course a notice of assessment is served on the person chargeable, and, if no objection is made within the time stipulated on such notice (viz., 21 days), the assessment is binding against him, subject to the right to claim repayment or adjustment in respect of exemptions, allowances, etc., within the times provided in the Acts. It is in the discretion of the Commissioners on reasonable cause being shown to allow an extension of the period named on the notice of assessment.

The income assessable under this schedule is set out below under the five headings appearing on the official form of return.

1. PROFITS OF TRADE, PROFESSION, EMPLOYMENT OR VOCATION. The assessment is made upon the amount of profits to be computed on an average of the three years ending either on the fifth day of April immediately preceding the year of assessment, or on the date prior to that day up to which the Annual Accounts have usually been made. If, however, the business has been set up or commenced within three years, the assessment is based on an average from the date of commencing the same, and, if commenced during the year of assessment, the profits are to be estimated according to the best information available and the assessment made accordingly.

The Income Tax Acts set out certain rules for arriving at the "statutory" income, and the following are deductions allowed, and not allowed, to be made from the profits and gains in arriving at this.

Deductions Allowed. (1) Repairs of premises

occupied for the purpose of the trade, etc., and the supply or repair of implements, utensils, or articles employed, not exceeding the sum usually expended for such purposes according to the average of the three years preceding.

(2) Debts proved to be bad; also doubtful debts according to their estimated value.

(3) The rent of premises used solely for the purpose of business, and not as a place of residence.

(4) A proportion of the rent of any dwelling-house partly used for the purpose of business.

(5) The annual value of any premises occupied by the owner solely for the purpose of business, and not as a place of residence, according to the amount on which duty has been paid under Schedule A; less ground rent, if any.

(6) Amounts paid as Excess Profits Duty and as Corporation Profits Tax.

(7) A proportion, not exceeding two-thirds, of the annual value (according to the amount on which duty has been paid under Schedule A); less ground rent (if any) of any dwelling-house occupied by the owner and partly used for the purpose of business.

(8) Any other disbursements or expenses *wholly and exclusively* laid out for the purpose of the trade, etc.

Deductions not Allowed. (1) Any interest on capital, any annual interest, annuity, or other annual payment, payable out of the profits or gains, or any royalty or other sum paid in respect of the user of a patent. (The duty on such interest, patent royalty, or other annual payment should be deducted from the person to whom payment is made.)

(2) Any sums paid as salaries to partners, or for drawings by partners.

(3) Any sums invested or employed as capital in the trade or business, or on account of capital withdrawn therefrom.

(4) Any sums expended in improvements of premises or written off for depreciation of land, buildings, or leases.

(5) Any loss not connected with, or arising out of the trade, etc.

(6) Any expense of maintenance of the persons assessable, their families, or establishments, or any sum expended in any other domestic or private purpose.

(7) Any loss recoverable under an insurance or contract of indemnity.

(8) Any sum paid as Income Tax on profits or gains, or on the annual value of trade premises.

(9) Wear and tear of machinery or plant, or for any premium for life assurance; but allowances may be claimed in respect of these items.

(10) Any repayment of Excess Profits Duty.

Commenting on these rules, the following observations may be made—

Doubtful Debts. Valuation of doubtful debts is allowed under Income Tax Act, 1918, Schedule D, cases i and ii, 3, the difference between the book value and the estimated value being a deduction allowed in arriving at the profits for Income Tax purposes.

Expenses "wholly and exclusively" laid out for the purposes of the trade, etc. The words "wholly and exclusively laid out for the purposes of the trade" have been taken from rule (3) to the first and second cases of Schedule D. They constitute a test that has been applied in many cases dealing with the right of deduction, and have proved a stumbling-block, even in cases where it would appear only equitable to allow the charge.

In the case of *Dillon v. Corporation of Haverfordwest* (1891) 3 Tax Cases, 31, where the Corporation owned gas works and supplied gas free for the public lamps, and supplied private consumers at a charge, it was urged the cost of lighting the public lamps was money "wholly and exclusively laid out for the purposes of a trade," and that the sum could be deducted in arriving at the profits from supplies to the private customers. It was held that it could not be so deducted, as the only trade carried on was that of supplying gas to private customers, in respect of which the outlay on public lighting was not laid out.

Damages and costs were paid by a brewery company to a guest at an inn owned by it, who had been injured by the fall of a chimney whilst sleeping at the inn. It was held that such expenses were not allowable as a deduction, as they were not wholly and exclusively laid out for the purposes of the trade. (See *Strong & Co. (of Romsey), Ltd., v. Woodisfield* (1906) 5 Tax Cases 215.)

Interest on Capital. Partners' Salaries and Drawings, Expenses and Maintenance of Persons Assessable, their Families, etc., and Income Tax. These items are not allowed, as they are apportionments of profits earned. For the same reason, general reserves made out of profits could not be deducted.

Annual Interest, Annuities and other Annual Payments. The Act directly charges the payer of Income Tax upon payments of this nature, but gives him the right to recoup himself by deducting tax when paying the recipient. The loss that otherwise would have been sustained by the non-allowance of such amounts as a charge in arriving at assessable profits is thus neutralised.

Depreciation of Land, Buildings, or Leases. A loss coming under this head is a loss of capital, and consequently is not allowed as a deduction. Where a ground rent is being paid in respect of leasehold premises, the amount of Schedule A assessment, or, in the case of mills, factories, etc., the full annual value, may be substituted as a charge in place of the ground rent. The additional amount so deducted would compensate,

more or less, for the inability to debit the lease depreciation.

Wear and Tear of Machinery and Plant. The Income Tax Act, 1918, Schedule D, cases i and ii, 6, deals with allowances that may be obtained in respect of this item of expense. The allowance is not fixed by statute, but is to be such amount that the Commissioners for General or Special Purposes consider represents the diminished value by reason of wear and tear during the year. The claim should be included in the return under this schedule, a space being reserved for the purpose in the official form. If full effect cannot be given to the deduction in any year owing to there being an insufficiency of profits against which to claim deduction, the amount, in respect of which effect cannot be given, may be taken into account in the following year, and so on for succeeding years. It will be found in practice that the Commissioners have a set scale of percentages upon which they arrive at the amount to be allowed, but they will usually consider any evidence produced, which proves that the allowance arrived at on the basis of the scale is insufficient, and make allowance accordingly. An allowance will not, however, be given if the effect of adding it to deductions allowed in previous years is to give a total exceeding the actual cost of the machinery and plant, including in that actual cost any expenditure in the nature of capital expenditure by the way of renewal improvements or reinstatements. It is now permissible for application to be made to a Board of Referees if any considerable number of persons engaged in any class of trade or business considers inadequate the amount allowed by the Commissioners for wear and tear. An allowance is also given for expenses incurred in replacing obsolete plant and machinery.

Hired Plant and Machinery which is scrapped and replaced. Plant and machinery, where hired and the hirer undertakes to maintain it and to deliver it back in good condition, is deemed to belong to such person, who may obtain an allowance accordingly. Where the true owner has to maintain the plant and machinery in good condition, he is entitled to the benefit of the claim, if claim be made within twelve months after the expiration of the year of assessment.

1. PROFITS INSUFFICIENT TO COVER ALLOWANCE FOR DEPRECIATION. The following is an example of full advantage not being able to be taken of an allowance for depreciation, and shows how the benefit is taken in the subsequent year.

A person derived the following profits from his trade during the four years ended 31st December, 1920, viz.—

Year 1917	.	.	.	£1,200
" 1918	.	.	.	600
" 1919	.	.	.	60
" 1920	.	.	.	3,900

The book value of his plant and machinery, which corresponded with the value as depreciated for Income Tax purposes at the end of 1919, was £20,000, upon which the Commissioners allowed a claim for the 1920-21 assessment at 5 per cent.

The Statutory Profits for 1920-21 (based on the average of the three years : 1917, 1918, and 1919) would be	£	620
The Depreciation Allowance—		
5% on £20,000		1,000
of which effect is not given to		£380

The assessment for that year will, therefore, be "nil," and the amount of £380 is taken into account in arriving at the 1921-22 assessment thus—

The Statutory Profits for 1921-22 based on the average of the three years : 1918, 1919, and 1920	£	£1,520
Less Depreciation—		
Balance of 1920-21 allowance	£380	
Allowance of 1921-22, viz.—		
5% on £19,000		950
		1,330
Amount assessable for 1921-22		£190

[NOTE. In the example given it has been assumed that there were no additions to plant and machinery in the year 1920; but had there been, the cost would have been added to the book value of the asset upon which the percentage is calculated.]

In practice, it will be found convenient to keep a separate memorandum account of plant and machinery depreciated at the rate allowed for Income Tax purposes, if such rate does not correspond with the percentage written off in the books of the business.

2. PROFITS FROM DISCOUNTS AND INTEREST OF MONEY NOT TAXED BY DEDUCTION. Under this head there fall to be assessed all discounts and untaxed interest received, including bank interest, and such dividends in the public funds from which tax has not been deducted. The assessment is upon the actual amounts arising therefrom in the previous year.

3. PROFITS FROM COLONIAL AND FOREIGN SECURITIES. Assessment on these profits is made under Schedule D, in such cases where they are not received through an agent who deducts British Income Tax before paying to the party entitled thereto. If tax has been deducted, the agent is liable to assessment under Schedule C (see above). Colonial and Foreign securities must not be confused with Colonial and Foreign Possessions. The income arising from the former is that received as interest, annuities or other annual payments from Indian, Colonial, and Foreign Government loans and railways and other public undertakings out of the United

Kingdom, not already taxed under Schedule C. The assessment is upon the full amount of income arising in the year of assessment, whether the income has been, or will be, received in the United Kingdom or not.

The following Deductions are Allowed. (1) Any sum paid in respect of Income Tax in the place where the income has arisen.

(2) Any annual interest, or any annuity or other annual payment payable out of the income to a person not resident in the United Kingdom.

The same deductions and allowances in the case of income not received in the United Kingdom, as if it had been so received.

4. PROFITS FROM COLONIAL AND FOREIGN POSSESSIONS. Income arising from stocks, shares, or rents is assessable upon the average of the three preceding years to the year of assessment, whether the same has been, or will be, received in the United Kingdom or not, and is subject, before assessment, to the same deductions referred to under the previous heading.

Other income arising from Colonial and Foreign possessions is liable to assessment upon the full annual amount received in the United Kingdom on the average of the three preceding years without any deduction.

Dealing with the income covered by the last two headings, the Finance Act, 1914, had an important bearing upon the treatment of income from abroad. Prior to the passing of that Act, income from the sources referred to not actually received in the United Kingdom was not assessable, and thus income could have been re-invested abroad without tax being chargeable. Even under the 1914 Act the income of a foreign business possessed by a resident in the United Kingdom escapes assessment if the control and management is situated abroad, to the extent that such income is re-invested abroad, except that where the re-investment is in stocks, shares, rents or colonial and foreign securities, the income arising therefrom is now assessable.

A point of contention between the taxpayer and the authorities is continually arising as to assessability of profits of a foreign business under case (1) or case (5) of Schedule D. If assessed under case (1) the whole of the profits of the business averaged for the preceding three years, whether remitted to this country or not, are assessable, as against only such amount as may have been remitted, similarly averaged, under case (5). It will be readily understood that the desire of the taxpayer, whose profits are accumulating in his business abroad is to be assessed under this last mentioned case.

The question for decision in these cases is that of (a) residence, or (b) direction and control. English companies with businesses abroad, if directed and controlled from this country, have

residence here, and are assessable under the first case. Even companies registered abroad may be chargeable with Income Tax under this case if the control and management is in the United Kingdom.

Residence. Temporary absentees are chargeable as residents, if they are away for the purpose only of occasional residence.

Temporary residents in the United Kingdom not with a view of establishing residence therein, are not chargeable with Income Tax in respect of income received from abroad, unless their residence has been for a period or periods equal to six months in the year. They are, however, assessable with Income Tax on any income derived in this country, and would, consequently, be liable to bear Income Tax in respect of property in this country whether occupied or owned by them.

Cases

(1) A master mariner trading between Glasgow and foreign ports, having a house for his wife and family in Glasgow, was held liable for assessment on his salary, notwithstanding he was abroad for the greater part of the year. (*In re Young* (1875) 1 Tax Cases 57.)

(2) A master mariner absent from the United Kingdom for the whole of the year, his wife and family living in a house belonging to him in the United Kingdom, was held liable to assessment under Schedule D of the Income Tax Acts as having a residence in the United Kingdom. (*Rogers v. Inland Revenue* (1879) 1 Tax Cases 225.)

(3) In the case of *Turnbull v. Inland Revenue* (1904) 42 Sc. L. R., it was held that a British merchant carrying on business in Madras, who had not been in the United Kingdom during the year of assessment, but whose family had resided in a house bought in his wife's name, was not chargeable as a resident in the United Kingdom.

(4) An American barrister, who leased a shoot in Scotland for a number of years, which he visited each year for about two months, was held to be a person "residing in the United Kingdom," and was accordingly assessed. (*Inland Revenue v. Cadwalader* (1904) 5 Tax Cases 101.)

(5) A foreigner, who lived on his yacht on the river Colne in Essex, was held liable as a person residing in the United Kingdom. (*Brown v. Burt* (1911) 5 Tax Cases 667.)

(6) A company registered in Norway owned a ship. Its meetings were held and its books kept there, but its agents at Glasgow effected all business connected with chartering and the finance relating to the boat. It was held that the company was not resident here, but carried on a trade in the United Kingdom and was assessable, as it exercised a trade within the United Kingdom. (*Wingate & Co. v. Webber* (1897) 3 Tax Cases 569.)

(7) In the case of *De Beers Consolidated Mines v. Howe* (1906) 5 Tax Cases 198, the company was registered in Cape Colony, but it was held that it

"resided" in the United Kingdom for the purposes of Income Tax. The sale of its diamonds on the London market was a factor in deciding this point.

(8) An English company working Italian sulphur mines, registered as an Italian company. The directors of the Italian company mainly controlled the business of the company, but the managing director of the English company was one of the Italian directors, and lived at the mines. The Italian directors were in constant correspondence with the English directors. It was held that the company was liable as a person residing in the United Kingdom in respect of the whole of the profits, as the directors held their meetings in the United Kingdom, and exercised the powers conferred on the company under the Companies Acts and its Articles of Association. (*Cesena Sulphur Co. v. Nicholson* (1876) 1 Tax Cases 88.)

(9) See also *Egyptian Hotels, Ltd. v. Mitchell* (1914), where only profits received in this country were assessable. (See next column.)

Direction and Control. The question of direction and control arises in cases of English companies holding the whole shares or sufficient shares to give a controlling interest in a foreign company.

(1) In the case of *St. Louis Breweries Co. v. Aphorpe* (1898) 4 Tax Cases 111, an English company acquired the whole (less thirteen shares required for the qualification of directors of the capital stock of an American company. The brewing manufacture was under the management of the directors of the American company and the books and accounts were kept in America. The accounts were audited there by an auditor sent over by the English company, the directors of which decided as to the dividend. The American company thereupon declared the amount decided upon. It was held that the business of the American company was carried on by the English company, and that the whole of the American company's profits were assessable under the first case.

(2) In *Kodak, Ltd. v. Clark* (1903) 4 Tax Cases 549, an English company acquired 98 per cent. of the shares of an American company, but had not the power to control the management of the American company, other than by voting as a shareholder. The remaining 2 per cent. of shares was held by independent parties. It was held that the business of the American company was not the business of the English company, and was not assessable under case (1), as the control exercised by the latter was only a control of shareholders.

(3) It was held in *Gramophone and Typewriter Co., Ltd. v. Stanley* (1908) 5 Tax Cases 358, that even the fact of an English company holding all the shares of a German company was not alone

sufficient in itself to make it assessable under case (1).

(4) In the case of *Egyptian Hotels, Ltd. v. Mitchell* (1914) 6 Tax Cases, it was held where the company had altered its Articles of Association so as to transfer to a local board in Egypt the absolute management and control of the Egyptian business, that case (5) applied, and only such amounts as were received in the United Kingdom were assessable.

From the above cases, it will be seen that residence is a question of fact to be decided in each instance, which, if existent, causes the resident to be liable to be charged with Income Tax on the following, in addition to the income of property, or of a trade, business, etc., carried on in this country.

(a) Income arising from any foreign securities, shares or rents, whether received in this country or left to accumulate abroad.

(b) The whole income arising from a business carried on abroad, if controlled and managed by the resident.

(c) Such income as is received in this country from a business carried on abroad, not controlled and managed by the resident.

But in the case of a person who is in this country for a temporary purpose only, and who owns foreign securities abroad, his income arising therefrom would not be assessable. If, however, his presence here amounted to a "residence," duty would be chargeable.

Residence and Partnerships. The residence in this country of a partner in a business controlled and managed abroad does not bring the residence of the business within the United Kingdom for the purpose of charging its profits with Income Tax. Only such profits as are received in this country by the residing partner or partners would be assessable if the whole business is carried on abroad, and, where part of the business consists of trading operations within the United Kingdom, the firm is assessable only on the profits of such operations to the same extent as a person resident abroad is assessable.

The assessment may be made in respect thereof in the name of any partner resident here.

The rule dealing with this point is Income Tax Act, 1918, Schedule D, cases i and ii, 12—

Sub-Section (1)—

"Where any trade or business is carried on by two or more persons in partnership, and the control and management of such trade or business is situate abroad, the said trade or business shall be deemed to be carried on by persons resident outside the United Kingdom, and the said partnership shall be deemed to reside outside the United Kingdom, notwithstanding the fact that some of the members of the said partnership are resident in the United

Kingdom, and that some of the trading operations of the said partnership are conducted within the United Kingdom." Subsection (2)—

"Where any part of the trade or business of a partnership firm, whose management and control is situate abroad consists of trading operations within the United Kingdom, the said firm shall be chargeable in respect of the profits of such trading operations within the United Kingdom, to the same extent as, and no further than, a person resident abroad is chargeable in respect of trading operations by him within the United Kingdom, notwithstanding the fact that one or more of the members of the said firm are resident in the United Kingdom, provided that, for the purpose of charging any such firm in respect of the profits of the said trading operations within the United Kingdom, an assessment may be made on the said firm in respect of the said profits in the name of any partner resident in the United Kingdom."

FOREIGN TRADERS AND AGENTS IN THE UNITED KINGDOM. A foreign trader who carries on a trade in this country is liable to assessment, even though the trade be carried on through an agent. Until 1915 the agent was assessable only if he had "the receipt of any profits or gains belonging to the foreign trader." The following cases, dealing with French wine merchants doing business in this country have a bearing on this point, but should be read in conjunction with the provisions which were first enacted in the Finance (No. 2) Act, 1915, and are duly incorporated in the Income Tax Act of 1918. (All Schedules, Rules 5-11.)

(a) In *Tischler & Co. v. Apthorpe* (1885) 2 Tax Cases 89, it was decided that, although not residents, the appellants were liable to tax, as they carried on a trade in the United Kingdom. One of the partners periodically visited this country at the firm's London agent's offices, where a room was rented by appellants.

(b) *Grainger & Son v. Gough* (1896) 3 Tax Cases 462. A French merchant appointed English agents, who were paid on commission, to obtain orders for wine, which were executed at the discretion of the merchant. Delivery was made from France, whence receipts for payments were sent. It was held that a trade was not exercised in the United Kingdom, and that profits were not assessable.

(c) *Pommery & Greno v. Apthorpe* (1886) 2 Tax Cases 182. The company here was held as exercising a trade in the United Kingdom, and were assessable in the name of their agents. Their English agent, who did no business other than for the French firm, held some of their stock for disposal, out of which he executed small orders, while the larger ones were delivered out of the

stock at Rheims. He received commission, out of which he had to defray office expenses.

Briefly, the effect of the rules referred to above is that a non-resident may be charged to Income Tax in the name of any branch or manager, as well as in the name of any factor, agent or receiver, even although such branch, factor, agent, receiver, or manager may not have the receipt of the profits or gains of the non-resident. Further, if a non-resident (not being a British subject or a British Indian, Dominion or Colonial firm or company or branch thereof) carries on business with a resident person, such non-resident may be chargeable to income tax if it appears to the commissioners that, owing to the close connection between the non-resident and the resident and to the substantial control exercised by the former over the latter, the course of business between the two is so arranged that the business done by the resident produces to him either no profit or less than the ordinary profit which might be expected to arise. If the profits cannot readily be ascertained the commissioners may make the assessment on a percentage of the business done through or with a resident. These rules do not apply to brokers or general commission agents, or to agents who are not the authorised persons carrying on the non-resident's regular agencies.

5. INCOME FROM PROPERTY OR PROFITS NOT FALLING UNDER ANY OF THE FOREGOING HEADS. Casual profits made in the carrying on of a business or occupation such as letting of furnished apartments would be included under this head, but generally it may be considered that casual profits made outside the course of usual business are not liable to assessment. Profits from isolated transactions on the Stock Exchange would, therefore, not be assessable, although the Commissioners would probably seek to assess those made from a series of transactions, as being made in the carrying on of a business.

ADJUSTMENT OF ACCOUNTS FOR INCOME TAX. It has been pointed out above that the assessment of businesses, professions, etc., is arrived at upon a basis of the average profits of the three years preceding the year of assessment, and that such profits must be arrived at having regard to the deductions allowed by statute. It is therefore evident that the accounts of a firm or limited company will require adjustment in order to arrive at the statutory income for insertion on the return for assessment under Schedule D.

In furnishing the Inspector of Taxes with accounts supporting a return, it is the usual practice to give copies of the Trading and Profit and Loss Accounts, as appearing in the books of the business, followed by a statement showing the adjustments that have been made in arriving at the "Income Tax" profit. This is of obvious assistance to the Inspector, as at a glance he can

see how the difference between the actual profits of a business and the statutory profits are arrived at. There is the alternative method of submitting an account from which expenses not chargeable against profits for Income Tax purposes are deleted, but it is not favoured by the Inspectors, as, amongst other things, it does not give any particulars as to the amount of interest paid which it is necessary to be known by the authorities in allowing relief in respect of earned incomes.

The following statement shows the figures of an imaginary trading business, whose accounts have been usually made up to the 31st December in each year, and which has been in existence for the three years ended the 31st December, 1920. This, being a date prior to the commencement of the Income Tax year ending 5th April, 1922, would be accepted as the basis for the 1921-22 return. As Trading Account items usually do not require adjustment, only the Profit and Loss Accounts are dealt with. (See next page.)

The following are comments upon the adjustments made above for Income Tax purposes, giving explanations as to the reason for making them—

1. *Ground Rent.* This amount is added to the profits as, in lieu thereof, the taxpayer is entitled to charge the Schedule A assessment of his business premises, as is shown on the debit side of the statement. (See List of Deductions allowed, given above.)

2. *Income Tax Schedules A and D.* Income Tax being considered an appropriation of the profits of a business and not a charge thereon (see List of Deductions not allowed) the debits in respect of these items have to be written back.

3. *Depreciation of Furniture and Utensils.* Actual renewals of furniture being allowed, if they are not in excess of the sum usually expended for such purpose according to an average of three years preceding the year of assessment, the depreciation may not be charged. The renewals for the different years are shown on the debit side of the statement.

4. *Depreciation of Plant and Machinery.* Wear and tear of plant and machinery is allowed by the Commissioners as a charge, but it should be noted that the allowance is in respect of the depreciation of the year of assessment, and not on the average of the three preceding years. Consequently, the amounts for depreciation charged in the accounts of the business have to be written back. In the illustration the starting value of the plant, etc., was assumed to be £400, from which 5 per cent., or £20, was written off in the first year, £19 in the second, and £18 in the third year. On the assumption that the authorities would consider 5 per cent. a reasonable allowance, depreciation at that rate would be allowed for the

fourth year (the year of assessment), £17, therefore, has been deducted from the average profits showing £1,395.

5. *Interest on Loans other than Bank Interest.* These amounts have to be added to the profits, as the payer is entitled to deduct tax on payment, and is accountable accordingly for the tax so deducted. It should be noted that, where interest on loans, other than on bank loans, is paid out of the profits of a business, the minimum amount of assessment is the amount of interest payable during the year of assessment after deducting any profits taxed at source (e.g.: dividends from investments). The object of making such interest the minimum charge is to ensure that the revenue receives the benefit of all tax deducted from interest. Thus, a business which makes no profits with which to meet its interest on loans has to do so out of capital. By the Income Tax Act, 1918, all Schedules, Rule 21, tax has to be deducted, although the interest so paid is not out of profits. An account has to be rendered to the Commissioners of the sum so deducted, which is payable to the Revenue. No hardship is caused to the taxpayer, as he only pays away an amount he has already received by deduction.

6. *Interest on Bank Loan.* Bank interest is allowed as a deduction from the profits of a business, where it is not annual interest, as Income Tax is not deducted by the bank before charging its customers. The Inland Revenue collect tax on such interest from the bank, who include it in their profits when returning them for assessment.

7. *Proprietor's Salary and Interest on Capital.* These items, being apportionments of the profits of the business, are not allowed as deductions. (See List of Deductions not allowed.)

8. *Dividends Receivable.* Tax having been deducted prior to receipt, such amounts are not again chargeable, and should be eliminated as shown.

9. *Profit on Sale of Investment.* The profit, being one of capital, is not assessable to Income Tax, unless the transaction is made in the ordinary course of the business, and is incidental to it.

Where the business of a concern is to buy stocks and shares, such a profit would be assessable to Income Tax.

BUSINESS SET UP WITHIN THREE YEARS OF THE YEAR OF ASSESSMENT. *Example 2.* The illustration may also be used to show how the assessable profits are arrived at where a business is set up within three years of assessment.

Assuming that the business had been set up on the 1st January, 1918, the first year's profits, as adjusted, viz., £1,645, would constitute the first year's assessment, and the practice is to utilise the same figure for the second year's

EXAMPLE (1).

PROFIT AND LOSS ACCOUNTS

	Year ended 31st December.				Year ended 31st December.		
	1918.	1919.	1920.		1918.	1919.	1920.
To Ground Rent	£ 25	£ 25	£ 25	By Gross Profits	£ 2,640	£ 2,142	£ 2,714
„ Income Tax (Schedule "A")	37	37	37	„ Dividends Receivable	15	15	12
„ „ „ (" " "D")	75	72	60	„ Profit on Sale of Investments	—	—	150
„ Rates	40	42	44				
„ Gas, Water, & Electric Light	50	55	60				
„ Insurances	10	10	10				
„ Trade Expenses	170	170	180				
„ Salaries	500	550	600				
„ Repairs	20	25	30				
„ Bad Debts	20	20	45				
„ Depreciation of—							
Furniture and Utensils	20	19	18				
Plant and Machinery	25	22	20				
„ Interest—							
On Bank Loan	50	50	50				
„ other Loans	100	100	100				
„ Proprietor's Salary	500	500	500				
„ Interest on Capital	150	150	150				
	1,792	1,847	1,929				
„ Net Profit	863	310	947				
	£2,655	£2,157	£2,876		£2,655	£2,157	£2,876

EXAMPLE (2).

INCOME TAX ADJUSTMENTS

	1918.	1919.	1920.		1918.	1919.	1920.
	£	£	£		£	£	£
To Dividends Receivable	15	15	12	By Net Profits as per A/cs	863	310	947
„ Profit on Sale of Investment	—	—	150	„ Ground Rent	25	25	25
„ Schedule "A" Assessment of Premises	125	125	125	„ Income Tax (Schedule "A")	37	37	37
„ Renewal of Furniture and Utensils	10	20	15	„ „ „ (" " "D")	75	72	60
	150	160	302	„ Depreciation of "Furniture and Utensils	20	19	18
				„ Depreciation of Plant, etc.	25	22	20
„ Adjusted Profits	1,645	1,075	1,555	„ Interest on Loans other than Bank	100	100	100
				„ Proprietor's Salary	500	500	500
				„ Interest on Capital	150	150	150
	£1,795	£1,235	£1,857		£1,795	£1,235	£1,857

Adjusted Profits for 1918	£1,645
„ „ „ 1919	1,075
„ „ „ 1920	1,555
Profits for three years	£4,275
One year Average	£1,425
Less Allowance for wear and tear of Plant and Machinery	17
Assessable Profits for 1921-22	£1,408

assessment. The taxpayer is entitled to have the actual profits of the second year, as adjusted for Income Tax, substituted, if appeal is made at the end of the year of assessment.

In the case above set out, as the profits of 1919 fell short of the previous year's profits upon which assessment would be made, appeal would be lodged, and £1,075 (the profits of the second year's trading) substituted for £1,645. The third year's assessment would be made upon the average of the first two years' profits, viz., £1,360, but as the actual profits of that year were in excess of this, no claim would be made. (See Income Tax Act, 1918, Schedule D, Cases i and ii, 8 (1).)

[NOTE. An allowance in respect of plant and machinery has not been taken into account in this illustration, although a claim would be allowed.]

Example 3. The following illustration gives figures of a manufacturing limited company, whose financial year ends on the 31st December in each year, and introduces points which arise in adjusting a company's accounts for Income Tax—

Comments on Example 3

(1) *Removal Expenses.* Expenses of removing a business to new premises are not allowable deductions. (See *Granite Supply Association v. Kitton* (1905) 5 Tax Cases 168.) In practice the above rule is not applied so rigorously. The cost of removing stock is sometimes allowed, as are other removal expenses if incurred compulsorily.

(2) *Bad Debts Reserve.* A sum of £1,000 being here added to the Reserve for Bad Debts, objection would be raised by the Inspector of Taxes to the amount being charged for Income Tax purposes, on the ground that the item is an apportionment of the profit. In this connection it may be mentioned that bad and doubtful debts are dealt with in the Income Tax Act, 1918, under the third rule of Cases i and ii of Schedule D, which provides that bad debts proved to be such to the satisfaction of the Commissioners may be deducted as expenses. Under the section above referred to doubtful debts may be valued, and the estimated loss allowed as a deduction from the profits.

(3) *Law Costs of Lease.* Such items are not allowed as charges against profits, as they are not expenses incurred in the carrying on of a

EXAMPLE (3).

PROFIT AND LOSS ACCOUNTS

	Year ended 31st December.				Year ended 31st December.		
	1918.	1919.	1920.		1918.	1919.	1920.
To Rent of Premises	£400	£400	£400	By Gross Profits	£15,000	£10,000	£17,000
„ Rates	125	130	135	„ Rents received	75	75	75
„ Trade Expenses, Salaries, etc.	2,500	2,450	2,600	„ Dividends	186	186	140
„ Income Tax (Schedule D) Balance ..	116	120	95				
„ Directors' Fees	1,000	1,000	1,000		15,261	10,261	17,215
„ Removal Expenses	—	1,250	—				
„ Bad Debts	175	325	290	„ Net Loss	—	677	—
„ „ Reserve	—	1,000	—				
„ Law Costs of Lease	45	—	—				
„ Debenture Interest	2,250	2,250	2,250				
„ Goodwill amount written off	500	500	500				
„ Depreciation of—							
Investments	—	1,200	—				
Plant and Machinery ..	200	190	180				
Furniture	25	23	20				
Lease	100	100	100				
„ Reserve Fund :							
Amount transferred ..	400	—	100				
„ Preliminary Expenses ..	600	—	—				
	£8,436	£10,938	£7,670				
„ Net Profit	6,825	—	9,545				
	£15,261	£10,938	£17,215		£15,261	£10,938	£17,215

INCOME TAX ADJUSTMENTS

	Year ended 31st December.				Year ended 31st December.		
	1918.	1919.	1920.		1918.	1919.	1920.
To Net Loss as per Account	£ —	£ 677	£ —	By Net Profit as per Ac/s ..	£ 6,825	£ —	£ 9,545
„ Rents received	75	75	75	„ Income Tax (Sched. D.)	116	120	95
„ Dividends received	186	186	140	„ Removal Expenses ..	—	1,250	—
	261	938	215	„ Bad Debts Reserve ..	—	1,000	—
				„ Law Costs of Lease ..	45	—	—
				„ Debenture Interest ..	2,250	2,250	2,250
				„ Goodwill amount written off	500	500	500
„ Adjusted Profits	10,800	5,695	12,575	„ Depreciation—			
				Investments	—	1,200	—
				Plant, etc.	200	190	180
				Furniture	25	23	20
				Lease	100	100	100
				„ Reserve	400	—	100
				„ Preliminary Expenses ..	600	—	—
	£11,061	£6,633	£12,790		£11,061	£6,633	£12,790

Adjusted Profits for 1918	£ 10,800
„ „ „ 1919	5,695
„ „ „ 1920	12,575
Three years' Profits	29,070
One year's Average	9,690
Less Allowance for wear and tear of Machinery ..	171
Profits assessable for 1921-22	£9,519

manufacturer's business. But if legal expenses are incurred in connection with recovering book debts, no objection would be raised to profits being debited with them.

(4) *Debenture Interest.* For reasons set out above in connection with interest on loans other than bank interest (see p. 957), debenture interest may not be charged as a deduction.

(5) *Goodwill.* The amount written off under this head must be written back, on the ground that it is a capital charge and not one of Revenue.

(6) *Depreciation of Investments and Leases.* These, being regarded as capital losses, the items may not be debited. But a set-off may often be obtained with regard to depreciation of leases by charging the Schedule A assessment against the profits instead of the rent payable under the lease. Thus, a lease of premises worth £100 per annum may be granted to a trader at an annual rent of £20, in consideration of a premium being

paid of £1,000. By substituting the Schedule A assessment of £100 for the rent paid £20, in preparing his accounts for Income Tax, the trader would be allowed a deduction of £80 per annum towards the capitalised rent paid in the amount of £1,000.

(7) *Reserve Fund Contribution and Preliminary Expenses.* Reserves are apportionment of profits, and cannot be claimed as a deduction. Preliminary expenses are disallowed as being a capital expense.

The following are points arising on the assessment of different businesses—

BREWERIES. (a) *Compensation Fund Charge* is allowed as a deduction. (See *Smith v. Lion Brewery Co., Ltd.* (1911) 5 Tax Cases 568.)

(b) *Losses on Loans to Tenants.* Cash loans by brewers to their tenants, if lost, may be charged against the profits of the brewery in arriving at the profits for assessment to Income Tax. (See *Reid's Brewery Co. v. Male* (1891) 3 Tax Cases 279.)

(c) *Repairs to, and Insurances, Rates and Legal Costs of, Tied Houses.* In the case of *Brickwood & Co. v. Reynolds* (1898) 3 Tax Cases 600, it was held that the excess of the cost of repairs of a tied house over the one-sixth allowed was inadmissible as a deduction in arriving at the Income Tax profits of the brewer. In the case of *Usher's Wiltshire Brewery Co., Ltd. v. Bruce* (1914) the Court of Appeal refused to allow as deductions any repairs to tied houses, or insurances, rates, taxes or legal costs in connection with them. Such expenses are allowed in the case of "managed" houses. And the House of Lords has reversed the decision of the Court of Appeal in the latter case, thus allowing that the expenses mentioned are costs incidental to the business of a brewer.

(d) *Extra Licence Duty.* This charge, although an expense appertaining to the public-houses belonging to or rented by the brewers, may be charged against the brewery profits in arriving at the Schedule D assessment. Following on this, it would appear equitable that payments for repairs to, rates and insurances of, tied houses, where borne by the brewers, should also be allowed, as has now been decided in the House of Lords. (See paragraph (c) relating to tied houses.)

(e) *Expenses of Applications for New Licences.* It has been held that these are expended on account of capital and are not chargeable as a deduction. (See *Southwell v. Savill Bros., Ltd.* (1901) 4 Tax Cases 430.)

(f) *Premium for Leases.* The case of *Watney & Co. v. Musgrave* (1880) 1 Tax Cases 272, decided that, where a brewer paid a premium for a lease of a public-house let to a tied tenant, he was not entitled to a deduction on account of the gradual exhaustion of the premium.

(g) *Damages for Injury.* In the case of *Strong & Co. (of Romsey), Ltd. v. Woodfield* (1906) 5 Tax Cases 215, it was held that, where brewers owned a hotel and carried on same as part of their business, they were not entitled to charge damages paid to a guest for injury by reason of a chimney falling.

INSURANCE COMPANIES. (1) *Unexpired Risks.*—

(a) *Fire Business.* A deduction in respect of unexpired risks was not allowed in the case of *Imperial Fire Insurance Co. v. Wilson* (1876) 1 Tax Cases 71, nor in the case of *General Accident Assurance Corporation v. McGowen* (1908) 5 Tax Cases 308, but in *The Sun Insurance Office v. Clark* (1912) 6 Tax Cases 59, a deduction was allowed by the Commissioners. In the House of Lords it was held that the deduction was a proper one, having regard to the Commissioners' finding of fact.

(b) *Life Business.* A deduction in respect of unexpired risks is allowed in this class of business.

(See *Scottish Union & National Insurance Co. v. Smiles* (1889) 2 Tax Cases 551.)

(2) *Annuities.* Sums paid by an Insurance company in respect of annuities were allowed as a charge in estimating the profits assessable under the first case of Schedule D. (See *Gresham Life Assurance Society v. Styles* (1892) 3 Tax Cases 185.)

(3) The case of *Last v. The London Assurance Corporation* (1885) 2 Tax Cases 100, decided that the business of an insurance company carrying on marine, fire and life insurance was assessable as a whole, and it was further held that in that case the bonuses paid to participating policy-holders could not be deducted in arriving at the assessable profits.

(4) An insurance company distributing its surplus of receipts over expenditure amongst its policy-holders (*i.e.* a mutual insurance company) was held not to be liable to assessment thereon. (See *New York Income Co. v. Styles* (1889) 2 Tax Cases 460.)

(5) But it was decided in a case where the London branch of an American Insurance Company had participating and non-participating policy-holders, the former entitled to a proportion of its profits after payment of expenses and a dividend to the shareholders, that the London profits were assessable. (See *Equitable Life Assurance Society of United States v. Bishop* (1909) 4 Tax Cases 147.)

(6) An insurance company carrying on both fire and life business was held liable to assessment upon its total profits and for that purpose the profits from both branches should be added together.

GENERAL. *Residence used for the Purpose of Trade, Etc.* A sum not exceeding two-thirds of rent if premises are let to the occupier, or of the amount of the Schedule A assessment if occupied by the owner, is allowed as a charge against the profits of the trade, etc.

Royalties (Patent). Payments in respect of these are not allowed as deductions. (See List of Deductions.)

Sinking Fund. It was held in the cases of *City of Dublin Steam Packet Co. v. O'Brien* (1912) 6 Tax Cases 101, and *Blake v. Imperial Brazilian Rail Co.* (1884) 2 Tax Cases 58, that a deduction for sinking fund was not permissible.

Bonus on Loan. Where a company undertook to pay, on the repayment of any capital sum, a bonus to the lender, it was held that such bonus could not be charged as a deduction. (See *Arizona Copper Co. v. Smiles* (1891) 3 Tax Cases 149.)

Expenses of Raising Capital. Commission paid to brokers and other expenses incurred in raising money by the issue of debentures cannot be deducted. (See *Texas Land & Mortgage Co. v. Holthan* (1894) 3 Tax Cases 255.)

Commutation of Salary. Such a payment was

not allowed in the case of *Royal Insurance Co. v. Watson* (1897) 3 Tax Cases 500, where the company had acquired the business of another insurance company with the undertaking to take into its service the manager of the acquired company, subject to the right to commute his salary by payment of a lump sum.

Unexecuted Contracts. Price paid for unexecuted contracts cannot be deducted from the profits arising from their performance. (See *City of London Contract Corporation v. Styles* (1887) 2 Tax Cases 239.)

Exhaustion of Assets. A claim to make deductions in respect of exhaustion of the deposits on land in Chili purchased by an English company was not allowed. (See *Alianza Co., Ltd. v. Bell*, 5 Tax Cases 172.)

Interest on Short Loans. In amplification of previous remarks concerning bank interest, it should be noted that interest, whether paid to a bank or otherwise, which comes under the head of annual interest as referred to in Income Tax Act, 1918, Schedule D, 1, is *not* allowed as a deduction, as the party paying the tax is entitled to deduct tax when making the payment, thus recouping himself for the additional amount of profits that are taxed by the interest not being deducted. As in the case of interest on short loans, no such rights to deduct tax arise, the payment is allowed as a charge.

Maintaining Profits of a Kindred Business. In the case of *Moore v. Stewarts & Lloyds* (1906) 43 Sc. L. R. (811) it was held that sums paid annually to make up the yearly profits of a kindred business, in consideration of receiving a controlling interest in the management of such business, were a proper charge in arriving at the assessable profits of the company making the contributions, as the payments had been made with a view to profit, and for the purpose of its trade.

Advances to another Company. In the case of *English Crown Speller Co. v. Baker* (1908) 5 Tax Cases 327, this company formed a new company for the purpose of obtaining its supplies of raw material, the shares being practically all owned by the parent company. The new company was not a success, and eventually went into liquidation, thereby causing a loss to the appellant company to the extent of advances made in excess of amounts due for raw material supplied. This loss had been written off as a bad debt, but it was held that the advances were an investment of capital and that the loss was not deductible in arriving at the profits of the company for assessment.

Compare this with the case of *Reid's Brewery Co. v. Male* (1891) 3 Tax Cases 279, mentioned above, where it was decided that losses on cash loans made by brewers to their tied tenants were deductible.

Loss of Capital. In a case where a new branch of a company was opened in Paris, and, on it being found unremunerative, was closed, and subsequently re-opened on a smaller scale, it was held that the amount claimed as a deduction in respect of the loss that arose on the construction of the new factory and putting up the machinery, was a loss of capital, and as such was not deductible (See *Smith v. Westinghouse Brake Co.* (1882) 2 Tax Cases 537.)

Expenditure with a view to Future Profit. The expenses of a rubber company for weeding, etc. that part of its land where the rubber trees had not come into bearing, were allowed, although that particular piece of the estate would not be yielding profits until future years. (*Vallambrosa Rubber Co. v. Farmer* (1910) 5 Tax Cases 529.)

Depreciation of Buildings. It was held in *Addie & Sons v. Solicitor of Inland Revenue*, 1 Tax Case 1, that depreciation of these was not allowable.

[NOTE. By the Income Tax Act, 1918, Schedule D, Cases i and ii, 5 (2), it is provided that where a trading concern owns its factories, mills, or other similar premises, it may be allowed to charge as an expense the *full* amount value of such premises instead of the Schedule A assessment of $\frac{1}{3}$ ths of the annual value.]

Subscriptions, Etc., to Trade Associations. (a) In *Rhymney Iron Co. v. Fowler* (1896) 3 Tax Cases 476, it was held that payments to an association for indemnifying its members against losses caused by strikes, etc., could not be deducted as a charge for Income Tax purposes, as they were not money laid out for the purpose of the trade.

(b) Payments by firms to a trade association for maintaining prices were allowed as a deduction from profits.

The members of this Association were entitled respectively to agreed proportions of total sales effected. The payments in the case given represented the contribution that had to be made in respect of sales effected over and above the proportion to which the member was entitled. (See *Guest, Keen & Nettlefolds, Ltd. v. Fowler* (1910) 5 Tax Cases 511.)

NOTE. In October, 1921, the National Union of Manufacturers gave public notice that the Union had entered into an arrangement with the Board of Inland Revenue, under which subscriptions, levies, donations, etc., paid by members and others may be allowed as a trade expense in computing their income tax liability.

Foreign Income Tax. This expense was allowed as a charge in the case of an English company working gold mines in Africa. (See *Stevens v. Durban Roodeport Gold Mining Co.* (1909) 5 Tax Cases 402.)

[NOTE. Under Income Tax Act, 1918, Schedule D, Case iv, 1, a deduction of Foreign Income Tax is

1. STATEMENT OF UNTAXED INCOME FOR ASSESSMENT UNDER SCHEDULE "D"

	Example A.	Example B.	EXPLANATORY NOTES
FROM TRADE, PROFESSION, EMPLOYMENT, OR VOCATION—			
The Trade, Profession, or Business of a Manufacturer, carried on by Mr. A. Blank, at 1 City Buildings, E.C. (a)	£1,425		(a) Assessment is here based on an average of the three years ended 31st December, 1920; and is the profit as adjusted before deducting the claim for depreciation.
The Employment or Vocation of A. Clerk carried on at London, E.C. (b)		£460	(b) Assessment is based on average of three years.
BANK OR OTHER INTEREST OF MONEY NOT TAXED BY DEDUCTION AND FROM DISCOUNTS, viz. (c)			(c) Profits to be inserted are the actual receipts of the year to 5th April, 1921.
(1) Interest on Bank Deposit	15	2	
(2) Dividend on £80 Consols	—	—	
(3) Interest on Post Office Savings Bank Account	—	3	
FROM COLONIAL AND FOREIGN SECURITIES (d)			(d) Figures to be given are amounts received or to be received, whether in the United Kingdom or not, in the year ending 5th April, 1922.
(where duty is not deducted by the Agent entrusted with payment thereof), viz.—			
Interest of Money, Annuities, or other Annual Payments arising from Railways out of the United Kingdom	None	None	
Interest of Money, Annuities, or other Annual Payments derived from Property out of the United Kingdom other than Railways	None	None	
Interest arising from Securities of Indian or Colonial Governments or Companies	None	None	
Interest arising from Foreign Securities	None	None	
FROM COLONIAL AND FOREIGN POSSESSIONS, viz.			
Possessions in any of His Majesty's Dominions out of the United Kingdom:			(e) Assessment is here based on actual receipts in the United Kingdom for three years to 31/12/20 (see <i>Colquhoun v. Brooks</i> (1889), 2 Tax Cases 490).
Receipts from share of profits in a business in Australia as sleeping partner (e)	150	None	(f) Assessment is here based on average of three years to 31/12/20, whether received in United Kingdom or not.
Possessions in Foreign Countries:			(g) Figures to be inserted here are the profits of the preceding year, when amount is fixed and certain; but, otherwise, the average is to be given.
Rents of property in Buenos Ayres (f)	500	None	
FROM PROPERTY OR PROFITS NOT FALLING UNDER ANY OF THE FOREGOING HEADS, viz.— (g)			
Letting furnished house at—	None	None	
Other Sources (the particular source to be stated,) viz.—	None	None	
	£2,090	£465	
Less Amount claimed for Wear and Tear of Machinery and Plant, which should not be deducted in arriving at the above figures	17	—	
NET TOTAL	£2,073	£465	

General Declaration.—I declare that in the foregoing statement I have given a full and true Return of the whole of the Income chargeable upon me under Schedule "D" of the Tax Acts, estimated to the best of my judgment and belief, according to the directions and rules of the said Acts. I desire to be assessed by the_____

Given under my hand this 10th day of May, 19..

_____ A. Blank or A. Clerk, _____ Signature.

_____ (see above) _____ Business Address.

_____ Suburbia, S.W. _____ Private Residence.

STATE WHETHER THE RETURN IS MADE: (1) On your own behalf; (2) as precedent Acting Partner of a Firm; (3) as Trustee, Agent, etc., for whom; (4) as Officer of any Corporation or Company.

[Note.—Return made on own behalf.]

allowed in respect of the income arising from securities, shares or rents in any place out of the United Kingdom.]

Improvement of Premises. The cost of these is not allowed as a charge. (See Official List of Deductions.)

Specimen Return under Schedule D. In order better to appreciate the assessment of the different sources of income under Schedule D, a specimen form for return of income under that schedule in respect of 1921-22 is here set out, filled in with figures of a manufacturer (Example A), and those of a clerk in receipt of a salary (Example B). The manufacturer's figures will be found to correspond with Example 1 given on page 963.

ALLOWANCES.—Having arrived at the total income from all sources, the taxpayer should then ascertain and deduct the allowances to which he is entitled. Until 1920 a system of abatement was in force, the amount of the abatement depending on the amount of the income. There was also a graduated rate of tax which again depended on the amount of total income. These, however, have been done away with, and the Finance Act, 1920 (adopting certain recommendations of the Royal Commission on the Income Tax), brought into operation for the year 1920-21 a radical alteration of the method of granting relief in the Income Tax in favour of earned income as compared with investment income, and of the method of graduating the burden of the tax according to the size of the taxpayer's income, and his family responsibilities. The exemptions, abatements and reliefs which previously existed are now replaced by the allowances dealt with in the following paragraphs. It should be understood that these allowances apply to individuals only, and not to Limited Companies.

Earned Income Allowance. Section 16 of the Finance Act, 1920, provides that, for the purpose

of ascertaining the amount of the assessable income of an individual for the purpose of income tax, an allowance of one-tenth of the earned income shall be made, but in no case must the allowance exceed £200. In other words, to arrive at the assessable income the taxpayer is entitled to deduct one-tenth of his earned income, but the deduction must not be more than £200. With the limitation referred to, the allowance can be claimed, no matter how large the earned income may be. It is further provided that if the total income of the taxpayer includes any *earned* income of his wife, the deduction is increased by nine-tenths of the amount of the wife's earned income, subject to the limitation that the additional allowance must in no case exceed £45. The effect of this provision is that the first £50 of the wife's earned income is not taxed.

Example—

Husband	.	.	.	.	£500
Wife	.	.	.	.	80
					£580
10 % Allowance	.	.	.	.	£58
Wife $50 \times \frac{9}{10} =$	.	.	.	.	45
					—
					103
Assessable Income	.	.	.	.	£477

Having arrived at the amount of the assessable income, the taxpayer proceeds to ascertain his taxable income by deducting such of the allowances referred to below as are applicable to his particular case.

Personal Allowance. An individual who proves that, for the year of assessment, he has his wife living with him, or that his wife is wholly maintained by him during the year of assessment, is entitled to a deduction of £225. In the case of an unmarried taxpayer, or one who does not fulfil

2. CLAIM FOR ALLOWANCE IN RESPECT OF LIFE ASSURANCE PREMIUMS, OR PAYMENTS UNDER CONTRACTS FOR DEFERRED ANNUITIES.

State whether the Assurance or Annuity is on life of "Self" or of "Wife."		Name of Assurance Company or Friendly Society.	Date of Policy or Contract.	* CAPITAL SUM PAYABLE AT DEATH—exclusive of any additional benefit by way of bonus or otherwise.	Amount of Premiums claimed as an allowance from the income returned on page 2.
Ex. A.	Self	Sound Insurance Co.	22 Jan., 1898	£2,000	£ s. d. 55 0 0
Ex. B.	Self	Prudent Insurance Co.	19 July, 1915	£100	2 12 0
	Wife	"	21 Aug., 1916	£100	1 8 0
				Total	£4 0 0

I claim an allowance in respect of the foregoing amount of premiums, and I declare that I have not deducted the amount of such premiums in arriving at the profits or gains entered on this form, and that I have not claimed an allowance for the premiums from any other assessment upon me.

* (If no CAPITAL SUM is payable at Death, particulars of the policy should be stated.)

-----Signature.

3. CLAIM FOR ALLOWANCE OR DEDUCTION

No. 1. PARTICULARS OF INCOME

	<i>Example A.</i>	<i>Example B.</i>	EXPLANATORY NOTES.		
FROM TRADE, PROFESSION, EMPLOYMENT, OR VOCATION—					
Profits from Business, etc., as returned for Schedule "D" assessment	£2,073	£465	See amounts returned above.		
FROM ANY PUBLIC OFFICE OR EMPLOYMENT NOT ENTERED ON PAGE 2 hereof (Name and address of Company, Corporation, etc.)			(a) This amount should be the gross amount before deduction of tax, and should be the income of the year 1921-22 taxed under Sched. E.		
Directors' Fees from Kylocks, Ltd. (a)	50	—	(b) This amount should correspond with the net Schedule A assessment.		
FROM PROPERTY (including annual value of pro- perty which I own and occupy)—					
1. Grove House, Park Road (b)	50	—			
2. House in own occupation (b)	100	—			
3. Business Premises in own occupation (b)	125	—			
FROM OCCUPATION OF LAND—					
Meadows in Blankshire—Rented (c)	20		(c) Schedule B. assessment, twice the gross annual value is to be given under this head.		
FROM BANK AND OTHER INTEREST, ANNUITIES, DIVIDENDS, OR OTHER INCOME NOT ALREADY ENTERED ON THIS PAGE (giving full particu- lars and stating whether taxed before receipt or not)—					
Interest on £1,000 loan at 4% taxed (d)	40	—	(d) Gross amount before deduction of tax to be included here.		
Dividend on £300 4% Johannesburg Stock— taxed (d)	12	—			
Dividend on £200 Great Eastern Railway Stock 4% Preference—taxed (d)	—	8			
WIFE'S INCOME, IF NOT INCLUDED ABOVE (giving full particulars, and stating whether taxed before receipt or not. If included above, it should be so stated; should there be no income from this source, the word "none" should be inserted)—					
Income received under Marriage Settlement Fund—5% on £2,000 Japanese Loan— taxed (e)	100	None	(e)	do.	do
	£2,570	£473			
No. 2. PARTICULARS OF CHARGES ON INCOME—					
Ground Rents—(f)					
1. House in own occupation £16			(f) do.		do.
2. Business premises 25					
Annuities—(g)					
J. Smith 200			(g) do.		do.
Patent Royalties None					
Interest on Mortgage or Loans—(h)			(h) This interest was payable out of business profits.		
5% on £2,000—Jones & Co. 100					
	341	—			
Total amount of Income, FROM ALL SOURCES less charges	£2,229	£473			

I declare that the above statement contains a full, just, and true account and return of the whole OF MY INCOME FROM EVERY SOURCE WHATSOEVER, for the year ending the 5th day of April, 1922, estimated according to the directions of the Income Tax Acts, and I therefore claim relief to which I am entitled in respect of such Income.

Given under my hand this ____10th____ day of _____May_____, 1921.

Signed_____A. Blank or A. Clerk,_____

Private Residence_____Suburbia, S.W._____

STATEMENT SHOWING METHOD OF ARRIVING AT ASSESSMENT OF UNTAXED INCOME
UNDER EXAMPLE "A" FOR 1921-22

The total net income of £2,229 should be analysed as follows—

	SCHEDULE "D" : UNTAXED INCOME.		INCOME TAXED UNDER OTHER SCHEDULES THAN SCHEDULE "D."	
	Earned.	Unearned.	Earned.	Unearned.
Profits from business	£	£	£	£
Less allowance for Wear and Tear	17			
Interest on Loan	100			
	1,308			
Interest on Loan paid from business has to be treated as "unearned" profit		100		
Profits from Discounts		15		
" from sleeping partnership in Australia		150		
" from foreign possessions in Buenos Ayres		500		
Directors' Fees taxed under Schedule "E"			50	
Income from Property as detailed on claim for abatement taxed under Schedule "A"				275
Income from occupation of land taxed under Schedule "B"			20	
Income from Interest, Dividends, etc., taxed by deduction			—	52
Wife's income, taxed by deduction			—	100
			£70	£427
Less charges as shown on return from which tax has been deducted				341
TOTAL NET INCOME	1,308	765	70	86

The following is an analysis of the total net income in Example "B"—

	SCHEDULE "D" : UNTAXED INCOME.		INCOME TAXED UNDER SCHEDULES OTHER THAN SCHEDULE "D."
	Earned.	Unearned.	Unearned.
Income from Employment	£ 460	£	£
" from Investment in Consols and Post Office Account received without deduction of tax		5	—
Income from Investment—tax deducted before receipt			8
Total Net Income	£460	£5	£8
	465		

To arrive at the assessable income, the earned income will be reduced by one-tenth. From the amount remaining will be deducted the allowances claimable by the taxpayer. This will leave the amount of "taxable" income which will be chargeable at 3s. in the £ on the first £225, and 6s. in the £ on the balance. Having arrived at the amount of the tax, the taxpayer will claim the assurance allowance at the appropriate rate.

the conditions just mentioned, the deduction is £135.

Example—

Assessable Income as above	£477
Allowances—Husband	£135
Wife	90
	<u>225</u>
Taxable Income	<u>£252</u>

Children's Allowance. If the taxpayer has at the commencement of the year of assessment any child who is either under the age of 16 years or who, if over that age, is receiving full time instruction at an educational establishment, he is entitled to a deduction of £36 in respect of one child, and £27 in respect of each subsequent child. The expression "children" includes a step-child, an illegitimate child, whose parents have married since its birth, and (where no one else claims the allowance) any other child maintained by the claimant. The deduction is not allowed in respect of any child who is entitled in his own right to an income exceeding £40 a year, but in calculating the income of the children no account is taken of income from a scholarship, bursary, or other similar educational endowment.

Example—

Assessable Income, £800 - 10 %	£720
Allowances—	
Husband	£135
Wife	90
Children, 36 + 27 + 27 =	90
	<u>315</u>
	<u>£405</u>

One child is over 16 but is attending school.

Relatives Taking Charge of Children. A widower who, for the year of assessment has resident with him for the purpose of having the charge and care of any children of his for whom the children's allowance is claimable, a female relative of his or of his deceased wife, is entitled to a deduction of £45 in respect of such female relative, or female person. The allowance can also be claimed if the taxpayer proves that he has no female relative of his own, or of his deceased wife who is able or willing to take such charge, and that he has employed some other female person to undertake the same. The above allowance can also be claimed by a widow in similar circumstances.

Example—

Assessable Income	£720
Allowances—Husband	£135
Female Relative	45
Children	90
	<u>270</u>
Taxable Income	<u>£450</u>

Widowed Mother. If an unmarried taxpayer has living with him for the purpose of having the charge of any brother or sister of his for whom the children's allowance can be claimed, either his mother who is a widow or living apart from her husband, or some other female relative, he is entitled to a deduction of £45, provided he maintains the mother or other relative at his own expense, and that no other person is allowed a deduction in respect of the same person.

Dependent Relatives. If the taxpayer maintains at his own expense a relative of his or of his wife, who is incapacitated by old age or infirmity from maintaining himself, he is entitled to a deduction of £25 for such person whose total income from all sources does not exceed £50 a year. A like deduction is allowed if the taxpayer, by reason of old age or infirmity, is compelled to depend upon the services of a daughter resident with, and maintained by him; and also if the taxpayer maintains at his own expense his, or his wife's, widowed Mother whether incapacitated or not, provided her total income from all sources does not exceed £50 a year. The provision applies to a female taxpayer similarly maintaining an incapacitated relative of her own, or of her husband.

When the relevant allowances have been deducted from the assessable income, the amount remaining is the taxable income, and this is chargeable, as to the first £225 at half the standard rate (at present 3s. in the £) and the remainder at the standard rate (6s. in the £).

Example—

Assessable Income	£720
Allowances—Husband	£135
Wife	90
Mother	25
Children	90
	<u>340</u>
Taxable Income	<u>£380</u>
£225 @ 3s.	£33 15
£155 @ 6s.	46 10
	<u>80 5</u>
Tax payable	

Life Assurance Premiums. The allowance made in respect of Life Assurance Premiums is deducted from the amount of tax as ascertained in the manner just indicated. The rules relating to deductions for Life Assurance Premiums are as follows—

Any person who insures his life, or the life of his wife, or enters into a contract for a deferred annuity on his own life or on that of his wife, is entitled to a deduction of the amount of the annual premium paid by him, provided the insurance is effected with a company legally established in the United Kingdom or in any British Possession

or lawfully carrying on business in the United Kingdom, or with a registered friendly society; or, in the case of a deferred annuity, with the National Debt Commissioners. Similarly, a person who is, under any Act of Parliament, or under the terms or conditions of his employment, liable to the payment of any sum, or to the deduction from his salary or stipend of any sum in order to secure a deferred annuity to his widow or a provision to his children after his death, is entitled to deduct from the tax payable by him, a sum representing tax at the appropriate rate on the premium paid by him, or on the amount of the sum paid by him, or deducted from his salary or stipend. The allowance must not exceed one-sixth of the total income of the taxpayer, nor in respect of any policy for securing a capital sum on death, 7 per cent. of the actual capital sum assured, but in calculating such capital sum all bonuses, participation in profits, etc., are to be ignored. If no capital sum is secured at death, no allowance may be made for that part of the premium which exceeds £100. Further, as regards assurances or contracts for deferred annuities made after the 22nd June, 1916, the allowance shall not be given at a greater rate than half the standard rate of tax, nor shall it be given in the case of a policy which does not secure a capital sum at death, nor in respect of premiums payable during the period of deferment in the case of a policy of deferred assurances. It is, however, provided that the last two restrictions shall not apply to policies or contracts made in connection with a superannuation fund, or *bonâ fide* pension schemes. Where a premium is paid by a wife out of her separate income, the same allowance shall be made as if the premium were paid by her husband.

The rate at which the allowance for assurance premiums is made is shown below—

In the case of all assurances or deferred annuity contracts made after 22nd June, 1916 . . . 3/- in the £

In the case of other assurances where the aggregate income does not exceed £1,000 . . . 3/- in the £

Where the aggregate income exceeds £1,000 but not £2,000 . . . 4/6 in the £ if the assurances were made on or before 22nd June, 1916.

Where the aggregate income exceeds £2,000 . . . 6/- in the £ if the assurances were made on or before 22nd June, 1916.

Marginal relief is allowed where the total income just falls short of £1,000 or £2,000. If the allowance is at a lower rate than it would have been if the income had not fallen short of these limits, the allowance is calculated as above, but it is increased by tax at 1s. 6d. in the £ on the premiums and decreased by tax at 6s. in the £ on the amount by which the total income falls short of the limit.

Example—

A. Williams, whose total income is £990, pays the following insurance premiums—

	Premium.
Deferred Annuity Policy, dated 12th Jan., 1912	£150
Life Policy, dated 15th Jan., 1917 (£400)	20
" " 1st Mar., 1919 (£400)	30
	<u>£200</u>

The allowance for the Deferred Annuity may not exceed £100, whilst the allowance in respect of the policy dated March, 1919, is restricted to £28 (7 per cent. of the sum assured at death)—the tax allowable in each case being at the rate of 3s. in the £.

The following example gives comparative incomes of £990 and £1,010 and shows the method of calculating the marginal relief—

	£	£
Total income (Earned)	990	1,010
Less 10 %	99	101
	<u>891</u>	<u>909</u>
Allowances— (Husband and Wife)	225	225
Taxable Income	<u>666</u>	<u>684</u>
Tax payable . . . £225 @ 3/- 441 @ 6/-	33 15 132 6	£225 @ 3/- 459 @ 6/-
	<u>166 1</u>	<u>171 9</u>
Less Assurance Premiums £100 + 20 + 28 = £148 @ 3/-	22 4	£100 @ 4/6 £22 10 48 @ 3/- 7 4
Total tax payable	<u>143 17</u>	<u>£141 15</u>
Adjustment— Premiums . . . £100 @ 1/6 Less (1,000-990) 10 @ 6/-	7 10 3 0	
Additional allowance . . .	<u>£4 10</u>	
Making tax payable	£139 7	as against £143 17

The allowance in respect of £48 may not exceed 3s. in the £ in any case as these policies were taken out after 22nd June, 1916.

ASSESSMENT OF PARTNERSHIPS. The examples set out above have dealt with businesses and vocations carried on by an individual or limited company, and it is now proposed to deal with Income Tax assessments made on partnerships, and the allocation of the tax paid between the partners of the firm.

Under the Income Tax Act, 1918, Schedule D, Cases i and ii, Rule 10, partners are assessed jointly in respect of the profits of the partnership, the firm being responsible for the tax. Section 20 of the 1918 Act, however, gives the individual partners the right to have their respective incomes from the partnership treated separately for the purpose of any claim for exemption, relief or abatement.

It will be appreciated that, having regard to

the fact that such items as partners' salaries and interest on capital usually appear in partnership accounts, the statutory profit of a partnership will not correspond with the annual profits divisible amongst the partners, and that owing to the partners being probably entitled to different shares of the profits, whether for salary, interest on capital, or share of balance of profits, the apportioning of the assessment correctly between the partners is important. Upon this depends the correct claim to relief, abatement or exemption of each partner, and the accurate allocation of the tax ultimately paid.

On p. 970 is an example of the treatment of partnerships profits for the purpose of Income Tax—

Three partners, A B and C, carry on a business. Their shares of the profits, after paying interest on capital and partners' salaries, were: A, one-half; B, one-third; and C, one-sixth.

This statutory profit is apportionable between the partners as follows—

(a) For that portion of the amount of such profit which is shown *before* adding the sums for partners' salaries and interest on partners' capital, in the proportion that the profits are divisible under the partnership deed.

(b) For the portion represented by the partners' salaries and interest on capital, in the proportion that such items are paid or credited to the partners.

The apportionment of the statutory profit of £3,350 of the firm given in the example would, therefore, be arrived at as shown in the statement set out on p. 970.

Assuming that the partners have no income other than that derived from the partnership, the assessment upon the firm for 1921-22 would be as appears on p. 970, subject to the allowances claimed by the individual partners.

TRADER, ETC., LIVING ON HIS BUSINESS PREMISES. On the Official List of Deductions given above, it is mentioned that deduction is allowed in arriving at profits for Income Tax for a proportion of the rent, not exceeding two-thirds, of any dwelling-house partly used for the purpose of business, or a similar proportion of the Schedule A assessment, less ground rent (if any), if occupied by the owner. The reason of the whole amount not being deductible is obvious, as an unfair advantage would be otherwise given to such traders, as compared with taxpayers living away from their business premises, who are not allowed to charge the rent of their houses when arriving at their "Income Tax" profits.

Similarly, only a proportion of rates and cost of lighting and water is allowed in practice. The following are illustrations of the adjustments made for Income Tax purposes of the accounts of a trader (a) living over business premises rented at £60 per annum, (b) living over his own premises assessed at £60 where ground rent of £10 is paid (p. 970.)

DOCTORS AND SOLICITORS. In the preparation of a doctor's accounts for Income Tax purposes, in addition to a proportion of the rent of his house being chargeable, a deduction may be made for the wages and keep of any page boy or domestic employed in connection with the practice. Deductions

PROFIT AND LOSS ACCOUNTS OF BUSINESS OF MESSRS. A B C & Co.

	1918.	1919.	1920.		1918.	1919.	1920.
	£	£	£		£	£	£
To Trade and other Expenses	2,950	3,250	3,550	By Gross Profit	6,000	6,600	7,200
„ Depreciation of—							
Furniture, etc.	25	25	25				
Lease	50	50	50				
„ Partners' Salaries—							
A	300	300	300				
B	450	450	450				
C	200	200	200				
„ Partners' Interest on Capital							
A	750	750	750				
B	400	400	400				
C	50	50	50				
	5,175	5,475	5,775				
„ Profits for Division	825	1,125	1,425				
	£6,000	£6,600	£7,200		£6,000	£6,600	£7,200

[NOTE.—It is assumed that item of expense—"Trade and other expenses"—are all chargeable for Income Tax purposes, and that no renewals of furniture have occurred during the three years covered by the accounts.]

INCOME TAX ADJUSTMENTS

	1918.	1919.	1920.		1918.	1919.	1920.
To Adjusted Profits . .	£3,050	£3,350	£3,650	By Profit brought down .	£825	£1,125	£1,425
				" Depreciation of Furniture, etc. . .	75	75	75
				" Profits before writing back Partners' Salary and Interest on Capital	900	1,200	1,500
				" Partners' Salary . .	950	950	950
				" Interest on Partners' Capital	1,200	1,200	1,200
	£3,050	£3,350	£3,650		£3,050	£3,350	£3,650

Adjusted Profits for 1918	£3,050
" " " 1919	3,350
" " " 1920	3,650

Profits for three years £10,050

One year's average being Statutory Profit of partnership for 1921-22 assessment £3,350

STATEMENT APPORTIONING STATUTORY PROFIT OF MESSRS. A B C & CO.

	Total Profit.	A.	B.	C.
Profits before writing back Partners' Salary and Interest on Capital (see above)	£	£	£	£
Year 1918	£ 900			
" 1919	1,200			
" 1920	1,500			
Three years	<u>£3,600</u>			
Average thereof	1,200	600	400	200
Partners' Salaries	950	300	450	200
Interest on Partners' Capital	1,200	750	400	50
	<u>£3,350</u>	<u>£1,650</u>	<u>£1,250</u>	<u>£450</u>

Each partner would claim the allowances due to him individually, and these would be deducted from the firm's assessment. Of the amount remaining, the firm would be charged on £225 for each partner @ 3s. in the £, and on the balance @ 6s. in the £.

	Illustration (a).	Illustration (b).
Profits as shown by accounts	£600	£650
Add: One-third of Rates (£18)	6	6
One-third of Water Rate (£3)	1	1
Lighting proportion applicable to private part of premises	10	10
Rent paid	60	10
	677	677
Less: Two-thirds of Rent paid	40	—
" of Schedule "A" assessment (£60)	—	40
Amount of adjusted profits to be brought into average	<u>£637</u>	<u>£637</u>

are allowed for the upkeep of a motor-car or cycle, rent of garage and wages of chauffeur.

It may be here mentioned that accounts of doctors are usually accepted, if prepared on a cash basis, as also are those of solicitors. Incipient charges are not usually taken into account.

PRODUCTION OF ACCOUNTS. When making a return of income assessable under this schedule, it is unusual to support the amount shown as income from a trade, business, etc., by production of accounts, unless so requested by the Inspector of Taxes, or for the purpose of appeal. It is a matter of controversy as to whether the Inspector can insist upon being furnished with accounts, but the Commissioners are empowered, when notice of appeal has been lodged, to direct the person appealing to return a schedule containing such particulars as the said Commissioners shall demand, respecting the property, trade, profession, etc., distinguishing the particulars of the deductions made from the profits earned. The Inspector has free access to such schedule, which would amount to a Profit and Loss Account for all practical purposes. The more convenient course is certainly to furnish the accounts, when asked for by the Inspector, as if he has any reason to doubt a return, a high assessment, or an additional assessment, if one has already been made, would eventually bring about an appeal by the taxpayer, who, in order to satisfy the Commissioners as to the excessiveness of the charge, would be compelled to support it by rendering accounts. A plea that such books are not kept as would enable a proper account to be prepared, does not assist a taxpayer, who thereby acknowledges the probable inaccuracy of his return, lays himself open to penalties, and places himself in the unenviable position of having to prove an assessment to be excessive without books to support his case. For the past few years requests have been made by Inspectors for the production of balance sheets, almost invariably in the case of limited companies, when the printed accounts with the directors' report are asked for, and frequently in the case of private firms. It can well be understood why they are wanted, as an examination of them would probably enable the Inspector to verify (a) the amounts written off for depreciation of machinery, plant, etc.; (b) the renewals of furniture and similar assets, where such renewals are claimed as a deduction in lieu of depreciation charged in the Profit and Loss Account; and (c) the amount of reserves charged against profits in the years under review. It is not, however, generally accepted that there exists any statutory provision in regard to their production, but, on the other hand, as most businesses in present times have accounts prepared, and as furnishing the balance sheet cannot have the effect of causing the taxpayer to be charged at

a higher figure than he legally should be, little objection can be put forward against its production, except on the ground of expense, which is generally more or less trivial. It will usually be found that a great deal of trouble and expense is saved by letting the Inspector have copies of such accounts as he may require, as many cases which otherwise would go to appeal before the Commissioners, can be settled in his office.

RETURNS BY EMPLOYED PERSONS. Returns made by employed persons should be carefully made, as the authorities have a check upon these, all employers being required by Section 105 of the Income Tax Act, 1918, to make a return of the name and addresses of persons employed by them whose incomes exceed the exemption limit, and of those whose incomes are below that amount, but have other employment.

Assessment under Schedule E. As in the case of assessment under Schedule D, a return is required to be made under Schedule E, which is followed by a notice of assessment in the latter part of the calendar year, when notice of appeal should be given if the charge is found to be excessive.

Assessment under this schedule is usually made upon the profits of the year of assessment, and covers all salaries, fees, wages, perquisites or profits relating to the following "public offices or employments of profit" within the United Kingdom.

(a) Any office belonging to either House of Parliament, Court of Justice, or any Criminal, Judiciary, or Ecclesiastical Court, or Court of Admiralty, Commissariat Court, or Court Martial.

(b) Any public office held under the Civil Government.

(c) Any commissioned officer in the Army.

(d) Any officer in the Navy, Militia or Volunteers.

(e) Any office held under an ecclesiastical body.

(f) Any office held under any Public Corporation or under any company or society, whether corporate or not corporate.

(g) Any office held under any public institution, etc.

(h) Any office in any county, riding, division, shire, or in any city, borough, town, corporate or place, or under any trusts or guardians of any fund or tolls.

(i) Every other public office or employment of profit of a public nature.

A case bearing upon the question as to what is "an office or employment of profit" was that of *Attorney-General v. Lancashire & Yorkshire Railway Co.* (1864) 10 L. T. 95. It was held that engine-drivers, porters and labourers were not persons holding "an office or employment of profit," but were assessable under Schedule D. Similarly, persons holding insubordinate positions in the employment of a company will not be

assessed on the salary of the year of assessment, if a claim is put forward to be charged on an average of the three years preceding the year of assessment, as under Schedule D. Company officials, however, are not allowed to average their income.

In the case of *Pickles v. Foster* (1913) 6 Tax Cases 131, it was held that, where any office or employment under any public corporation or company is exercised abroad, the income arising therefrom cannot be assessed under Schedule E.

Under Income Tax Act, 1918, Schedule E, Rule 18, however, a person holding an office under a "department" is deemed to exercise his duties at the head office of the department, although they may be performed out of the United Kingdom. In the case just referred to, the employment of the appellant was not held under a department.

Clergymen are assessed under Schedule E in respect of Easter offerings (see *Blakiston v. Cooper* (1909) 5 Tax Cases 347), but where they were given to an incumbent on account of his poverty, it was held he was not assessable, as they were not given as an additional remuneration for services. (See *Turton v. Cooper* (1905) 5 Tax Cases 138.)

The "perquisites" above referred to are described by Rule (4) to the schedule, as being "such profits of offices and employments as arise from fees or other emoluments, and payable either by the Crown or the subject, in the course of executing such offices or employments." Income of this nature may be estimated on the profits of the preceding year or on an average of three years.

DEDUCTIONS ALLOWED FROM INCOME. (1) *Expenses* necessarily incurred in the performance of any public office or employment, the income of which is assessable under this schedule, are to be deducted in arriving at the amount assessable. These cover travelling expenses in the performance of the duties required and expenses of keeping or maintaining of a horse for such purpose. (See Income Tax Act, 1918, Schedule E, Rule 9.)

(2) Where the Treasury are satisfied with respect to any class of person in receipt of any salary, etc., payable out of the public revenue, that such persons are obliged to expend money wholly in the performance of the duties, the Treasury may fix such a sum as they may consider a fair equivalent of the average annual amount so expended. The sum so fixed shall be deducted as an expense (Income Tax Act, 1918, Schedule E, Rule 10). A person who otherwise would be entitled to deduct a larger amount than the sum so fixed, is allowed, under the Section referred to, to have the larger amount deducted.

(3) *Travelling Expenses* of directors from home to their company's offices were not allowed in the case *Revell v. Directors of Elworthy Bros. &*

Co., Ltd. (1890) 3 Tax Cases, 12, nor were those of a solicitor incurred in travelling from his office at Worcester to Bromyard, where he acted as Clerk to the Justices. (See *Cook v. Knott* (1887) 2 Tax Cases 246.)

(4) *Minister's Expenses.* In *Jardine v. Gillespie* (1907) 5 Tax Cases 263, it was held that the cost of keeping a horse and carriage, and an allowance for communion elements were correct deductions, but cost of pulpit supply during his holidays, and expenses of obtaining augmentation of stipend were disallowed.

The Income Tax Act, 1918, all Schedules, Rule 12, deals with expenses under this heading, the former allowing abatement to clergymen or ministers for expenses "wholly, exclusively and necessarily" incurred in the performance of their duty as such, and also a part of the rent of the dwelling-house, not exceeding one-eighth, to be treated as a deductible expense, if a part of the house is "mainly and substantially" used for the purpose of their duty. If a clergyman or minister occupies a dwelling-house but pays no rent therefor the allowance referred to above is based on the Schedule A assessment of the house.

ASSESSMENT FOR SUPER-TAX.—Super-tax is an additional duty of Income Tax, charged on all incomes exceeding £2,000 of any individual, the income here referred to being the total statutory income from all sources estimated in the same manner as the total income from all sources is estimated for the purpose of exemptions or abatements, but subject to certain provisions referred to below. It will be observed that this tax only refers to "any individual," which term, as has been already explained, does not include companies, corporations, etc.

The assessment is based upon the income of the year preceding the year of assessment. In estimating the income of the previous year for the purpose of Super-tax, Section 5 (3) of the Income Tax Act, 1918, provides—

"(a) There shall be deducted in respect of any land on which Income Tax is charged upon the annual value estimated, otherwise than in relation to profits (in addition to any other deduction) any sum by which the assessment is reduced for the purposes of collection, or on which income tax has been repaid under the provisions of this Act in respect of the cost of maintenance, repairs, insurance and management; and

"(b) there shall be deducted in the case of a person in the service of the Crown abroad, any such sum as the Treasury may allow for expenses which in their opinion are necessarily incidental to the discharge of the functions of his office and for which an allowance has not already been made;

"(c) Any income which is chargeable with

Income Tax by way of deduction shall be deemed to be income of the year in which it is receivable, and any deductions allowable on account of any annual sums paid out of the property or profits of the individual shall be allowed as deductions in respect of the year in which they are payable, notwithstanding that the income or the annual sums, as the case may be, accrued in whole or in part before that year."

From the above, it will be seen that the income assessed to Super-tax includes income from all sources, whether charged with Income Tax by way of assessment, or by way of deduction. As the statutory income of the year preceding the year of assessment is assessable, the period upon which it is based will vary according to the Schedule or Case under which the statutory income is arrived at. Thus—

(a) If derived from a business, profession or vocation, the income would be based upon the profits of the three years prior to the year preceding the year of assessment; thus, the basis for the 1921-22 assessment would be the profits of the years 1917, 1918, and 1919. (The Income Tax assessment of 1920-21.)

If, however, such business, etc., had been set up within three years of the year preceding the year of assessment, the income might be based on either the profits of the year preceding the year of assessment, or the average of the two years prior to the year preceding the year of assessment.

(b) If receivable from dividends, it would be based upon the previous year's receipts, as would also such amounts as were derived from director's fees or Foreign and other securities chargeable under Case (4) of the Schedule D.

(c) If received from foreign possessions assessable under Case (5), it would be based upon the average of the three years prior to the year preceding the year of assessment.

All usual Income Tax charges on income, viz., ground rents, annuities and annual interest should be deducted from the income of the taxpayer in arriving at the total income for Super-tax purposes in addition to which the following special deductions are allowed.

The 10 per cent. allowance for earned income does not apply for Super-tax purposes.

Special Deductions Allowed for Super-Tax. (1) Under Income Tax Act, 1918, Section 5 (3a), the "one-eighth" and "one-sixth" allowance for REPAIRS, etc., by which the assessment of any lands or buildings is reduced.

(2) Under the same paragraph the allowance on which duty has been repaid under Income Tax Act, 1918, Schedule A, v, Rule 8. The allowance, here referred to, is that made when it is shown to the Commissioners of Inland Revenue

that the cost of maintenance, repairs, insurance and management, averaged on the cost of the five preceding years, of any land (inclusive of farm-houses and other buildings, if any), the assessment of which is reduced, or of any houses the annual value of which under Schedule A does not exceed in London £105, Scotland £90, and elsewhere £78 has exceeded the one-eighth and one-sixth reduction allowed from the gross assessments.

(3) EXPENSES incidental to the discharge of the office of a person in the service of the Crown as allowed by the Treasury.

The assessment to Super-tax is different from that to the ordinary Income Tax in several particulars, of which the following are the chief—

(1) The charge for Super-tax is on individuals only, corporations, including companies, societies, etc., not being chargeable. To ordinary Income Tax, all "persons" are charged, other than those especially exempted. (See previous definition of "person.")

The assessment in respect of which tax has been paid for the year preceding the year of assessment usually determines the amount to be entered as income taxed by way of assessment, but in the case of *Wylie Hill v. Commissioners of Inland Revenue* (1912) (49) Sc. L. R. 960, where the appellant had not claimed relief under Section (23) of the Customs and Inland Revenue Act, 1890, in respect of losses on farms occupied by him, it was held that for the purpose of the Super-tax assessment he was entitled to claim the losses in question.

Income taxed by way of deduction should be included in the return at its gross amount in the same way as would be done when filling up a claim form for abatement relief or repayment.

On page 974 is a specimen return for Super-tax in respect of the years 1921-22, with explanatory notes.

Super-tax would be payable on this amount as it is in excess of £2,000, as follows—

	£	s.	d.
On £2,000	Nil	0	0
" 500 @ 1s. 6d. in the £	.	37	10
" 500 @ 2s.	" "	50	0
" 840 @ 2s. 6d.	" "	105	0
		<u>£192</u>	<u>10 0</u>

Partnership Profits and Super-tax. Where part of the income consists of a share of profits from a partnership, care has to be exercised in arriving at the proper amount to be entered in the return for Super-tax. The Inland Revenue authorities, recognising the difficulty likely to be experienced, through the Special Commissioners for Income Tax issue the following supplementary information for the guidance of persons in respect of

SPECIMEN SUPER-TAX RETURN, 1921-22

No. 1. PARTICULARS OF INCOME—

(a) *From Trade, Profession, Office, Employment, or Vocation, viz.—*

Statutory Income of "Trading Business" . . . £2,200

Directors' Fees from Kylocks, Ltd. . . . £300

(b) *From Property (including the annual value of the property which I own and occupy—*

(1) Broadlands—Norfolk £100

(2) House in own occupation £120

(c) *From Occupation of Land* None(d) *From Bank and other Interest, Annuities, Dividends, or other Income not already entered on this page—*

Sundry—Taxed £300

Interest on Loans—Taxed £550

(e) *From Wife's Income (giving full particulars)*

Sundry Dividends £350

Total £3,920

No. 2. PARTICULARS OF ANY CHARGES ON INCOME—

Less Ground Rents of Properties . . . £30

„ Interest payable on Loans . . . 50

£80

Total Income, less charges £3,840

Total Income for Super-tax purposes £3,840

EXPLANATORY NOTES

{ The Statutory Income included is that of the 1920-21 assessment, (i.e. based on the average of the three years, 1917, 1918, 1919).

{ Income taxed under Schedule "E," for 1920-21 assessment based on the fees of that year.

{ Entered at Net Schedule "A" assessment (Ground Rent included below under Annual Charges).

{ Gross amount received in year ended 5th April, 1921 before deduction of tax to be entered.

do. do.

{ Ground Rents and Interest: Gross amounts for 1920-21 to be entered.

Partnership income as assessed for the year 1918-19 (say) Average profits 1915-16, 1916-17 and 1917-18

£20,000

Partnership income receivable in the year from: (a) Dividends upon investments; (b) interest; (c) rents; (d) annual value of premises (see above); and (e) any other source of taxed income (say)—

Dividends upon investments £2,500

Interest upon Loans 2,500

Rents 2,500

Annual Value of Premises owned and occupied by firm (i.e. the net Income Assessment,

Schedule "A") 2,500

10,000

Total Income for Income Tax purposes

30,000

If a firm made any payments to third persons in respect of, for instance: (a) Ground rents; (b) annual interest on mortgage or other loans to the firm; (c) annuities payable out of profits, these should be claimed as deductions from the above as follows (say)—

Ground Rents £1,000

Annual Interest 1,000

Annuities payable out of profits 1,000

3,000

Leaving £27,000

£27,000

partnership profits liable to Super-tax, in addition to the directions given on the form of return for Super-tax—

Such profits are to be returned for assessment to Super-tax for the year 1919-20, on the basis of

the Income Tax assessments made for the year 1918-19. To avoid misconception, it should be remembered—

1. That an Income Tax assessment under the rules of Schedule D made upon a firm is not made

upon the actual profits of the year, but upon the average of the profits of the prescribed number of previous years, and that the profits actually realised in the year of assessment may be either more or less than such assessment.

2. That such assessment is made *exclusive*—

(a) Of any rents of property received by the firm, and of the annual value, as assessed to Income Tax, Schedule A, of premises owned or occupied by them ;

(b) Of any other taxed income received by the firm.

Such assessment, however, includes partners' salaries and interest, royalties and other annual payments paid to partners and other persons out of the profits of the firm.

From these two considerations, it follows that the whole income of the firm, as described in the above paragraphs, should be reviewed by a partner in computing his return for Super-tax, and that the interest and charges should be adjusted as shown in the illustration on page 994.

A firm consisting of three members (A, B, and C) might have £27,000 available, which represents the sum which, for Super-tax purposes, is to be treated as divisible among the partners of the firm.

Supposing, therefore, that in the year 1918-19, under the deed of partnership, partner "B" is entitled to a salary of £1,000 as a first charge on the partnership profits, and that the capital of the firm, amounting for that year to (say) £60,000, held equally by the partners, is next directed to be credited with interest at 5 per cent. per annum, and that the balance of the profits is divisible in the proportion of : A five-tenths, B three-tenths, C two-tenths, then the income from the partnership of each member of the firm for Super-tax purposes for the year 1919-20 would be as shown below—

These sums of £12,500, £8,900 and £5,600 represent the amounts such partners A, B and C respectively are, for Super-tax purposes, to be considered to have derived from this business, and should be entered by them in their several returns.

Partners who have borrowed on their personal security money which they have put into the business, should not treat the interest they pay thereon as a deduction in arriving at their share of the partnership profits for insertion in the space on the form of return for "particulars of income," but such interest should be claimed as a deduction in the space reserved for particulars of any charges on income.

From the above information, it will be seen that the rules to be observed in arriving at the amount to be included in a Super-tax return of a particular partner are—

1. Take the statutory profit of the partnership of the preceding Income Tax year (*i.e.* the amount based upon the figures of the three years immediately prior to that year, if the profits assessable are derived from a trade, profession, etc.

2. Add to that figure the taxed income of the partnership, whether from dividends, interest or occupation of premises owned by the firm in respect of the preceding year.

3. From the total of profits included under headings 1 and 2 deduct—

(a) Annual charges of the partnership, viz., ground rents, annuities, royalties (patent) and interest on loans paid in the preceding year.

(b) Partners' salaries and interest on partners' capital.

4. The amount then shown is the amount to be considered as divisible in the proportions determined by the partnership deed.

5. Ascertain the particular partner's share of the amount considered as being so divisible, and add to it the amount of interest on his capital and the

Partnership Income for Super-tax purposes, as shown above	.	.	.	.	.	£	27,000
Less Managing Partner's Salary	.	.	.	.	.	£1,000	
Interest on Partners' Capital (£60,000 @ 5%)	.	.	.	.	.	3,000	
							4,000
Amount proportionately divisible among the Partners	.	.	.	.	.		£23,000

	PARTNERS.		
	A.	B.	C.
Interest on Capital	£1,000	£1,000	£1,000
Share of Profits	5/10ths 11,500	3/10ths 6,900	2/10ths 4,600
Salary .	—	1,000	—
	£12,500	£8,900	£5,600

salary that he is entitled to for the preceding year, the result being the amount for insertion in the return.

MARRIED WOMEN.—The income of a married woman living with her husband, where application has not been made under Income Tax Act, 1918, all schedules, Rule 17, is charged on the husband, their joint incomes being treated together for the purposes of aggregation for exemption, abatement, or Super-tax.

It is provided, however, that if application is made either by a husband or wife within six months before 6th May in any year of assessment, income tax for that year shall be assessed and charged on the income of the husband and on the income of the wife, separately, but it should be noted that this method of assessment does not serve to reduce the amount of tax which would have been payable had the assessment been made on the husband only. The effect of this section is that the allowances claimable are apportioned between the husband and wife in the following manner—

(1) The earned income relief is given in proportion to the respective *earned* incomes of husband and wife.

(2) The personal allowance, marriage allowance, children's allowance, and the reduced rate of tax on the first £225 of taxable income, are given in proportion to the respective *assessable* incomes of husband and wife.

(3) Deductions in respect of an adopted child or dependent relative are given to the person supporting the child or relative.

(4) An allowance of Life Assurance premiums is given to the person paying the premium.

SUPER-TAX.—The claim for separate assessment applies also in the case of super-tax.

INFANTS AND OTHER INCAPACITATED PERSONS.—(1) A Minor is liable to assessment in the name of his legal representative. The guardian, as his representative, is answerable for the doing of all things required by the Income Tax Acts in order to bring about the correct assessment of the minor's income. He has to make returns or claim abatements or exemption, if the income comes within the specified limits.

An interesting point arises in connection with a claim to abatement or exemption, as to whether the minor's interest in the income is an absolute or vested interest, or merely contingent, that is, conditional upon the happening of some event, such as reaching a particular age. In the former case, a claim to exemption or abatement is allowed, but until 1917, not where the interest was contingent, except that, if part of the income had been properly expended on the maintenance or education of the infant, the claim to relief would be allowed, but was restricted to such actual expenditure. Even on the happening of the event, when the interest became absolute, the authorities would

not allow a claim in respect of the "contingent" period.

This matter received attention in the Income Tax Act, 1918, Section 25, of which reads as follows—

"Where in pursuance of the provisions of any will of settlement any income arising from any fund is accumulated for the benefit of any person contingently on his attaining some specified age or marrying, and the aggregate amount in any year of assessment of that income and the income from any other fund subject to the like trusts for accumulation and of the total income of that person from all sources (hereinafter referred to as 'the aggregate yearly income') is of such an amount only as would entitle an individual either to total exemption from tax or to relief from tax, that person shall, on making a claim for the purpose within three years after the end of the year of assessment in which the contingency happens, be entitled, on proof of the claim in manner prescribed by this Act, to have repaid to him on account of the tax which has been paid in respect of the income during the period of accumulation a sum equal to the aggregate amount of relief to which he would have been entitled if his total income from all sources for each of the several years of the said period had been equal to the aggregate yearly income for that year; but in calculating that sum a deduction shall be made in respect of any relief already received."

(2) **Lunatics, Idiots, and Insane Persons** are assessed in the name of their legal representatives, who are chargeable to the duties upon the income of such persons, and may make claims for abatements or exemption on their behalf.

(3) **Non-Residents**, in so far as income is received by them from property, or a trade, etc., exercised within the United Kingdom, are assessable in the name of their agents, whether such agents have the receipts of any profits or gains of the non-residents or not. Agents thus assessed are entitled to recoup any duties paid by them out of any moneys belonging to their principal that may be in their hands.

(4) **Deceased Person.** Executors or administrators of a person who dies are liable to pay duties chargeable on the deceased, and the amount so paid by them may be recouped by them out of the estate. If no return has been made by the deceased, they may be assessed in respect of the profits and gains, which accrued before his death, any time within the year of assessment or within three years after the expiration thereof.

Under Income Tax Act, 1918, Schedule D, Miscellaneous 3 (1), application may be made to the Commissioners by the executor or administrator for an adjustment of the assessment, and for such

relief as may be just, and under Income Tax, 1918, Schedule D, Cases i and ii, 8 (1), if the death causes the discontinuance of a trade, etc., an adjustment of assessment to the actual profits arising in the year of assessment may be obtained, or a repayment of tax upon such amount as may have been overpaid during the three previous years, when compared with the actual profits of those years.

The assessment will be reduced by the 10 per cent. allowance and the personal allowance of £135.

Super-tax, as regards deceased persons, is dealt with under Income Tax Act, 1918, Section 6, which provides that only the proportionate part of the year's super-tax shall be paid as corresponds with the part of the year which has elapsed before the date of death.

Example. A person whose Super-tax assessment for 1921-22 is £3,840, dies on 5th Oct., 1921. The tax for the full year is £192 10s., but half of this amount only will be payable.

CAPITAL PROFITS AND LOSSES.—The first-mentioned are not assessable, and capital losses are not allowed as a deduction in arriving at the assessable profits for assessment purposes.

Capital profits would include those as may be received on the sale of investments, where dealing in securities is not part of the business of the person to be assessed.

The profits made on sale of investments by a trust company, which makes a practice under power of its Memorandum of Association of realising securities, are assessable to Income Tax thereon. Depreciation of other securities may not be charged in arriving at the amount upon which assessment should be made. (See *Scottish Investment Co. v. Forbes* (1893) 3 Tax Cases 231, and *Northern Assurance Co. v. Russell* (1889) 2 Tax Cases 571.)

Examples of Capital Profits and Losses. (1) If a firm or business disposes of any of its capital assets (such as its buildings, its plants and machinery, or its lease of premises) and makes a profit, this would be regarded as a capital profit, and would not be assessable.

(2) A company purchased an estate for the purpose of producing rubber. It proceeded to develop it, intending to bring it into bearing and selling the produce for the benefit of its shareholders. The rubber boom came along, and, taking advantage of the market, the company disposed of its whole concern and realised a substantial profit over and above the cost of the estate and all outlay thereon in connection with developing it. No Income Tax was charged on the profit.

(3) If, however, a syndicate had purchased the estate with a view to selling it as a whole, and a profit had been realised under similar circumstances, the profit would be assessable.

Gifts received (*i.e.* receipts in respect of which

no consideration is, or has been given) are not assessable to Income Tax, and even where they take the form of a voluntary annuity, they will not be charged with duties unless it is given under a deed or in respect of past services (*e.g.* a retiring allowance made to an old clerk or servant).

CAPITAL EXPENDITURE.—Payments of this character are not allowed as a charge against profits for Income Tax purposes under Section (100) of Schedule D, 1st Case, Rule 3, and Section (159) of the 1842 Act. A number of cases on this subject have been referred to above under the heading of "Deductions," viz., *Reid's Brewery Co. v. Male* (1891), see page 960; *Southwell v. Savill Bros.* (1901), see page 961; *Watney v. Musgrave* (1880), see page 961; *Royal Insurance Co. v. Watson* (1897), see page 962; *Alianza Co., Ltd. v. Bell*, see page 962; and *City of London Contract Corporation v. Styles* (1887), see page 962.

NON-RESIDENTS AND ALLOWANCES.—Generally, the allowances in respect of earned income, the personal allowance, marriage allowance, allowance for children and dependent relatives, and the allowances for life assurance premiums are granted only to residents in the United Kingdom. Exceptions are made in the case of any person who is, or has been employed in the service of the Crown, persons in the service of any missionary society abroad, or in the service of any of the native states under the protectorate of the British Crown. Residents in the Isle of Man and the Channel Islands are also excepted and any person formerly resident in the United Kingdom who resides abroad for the sake of health, and any widow who is in receipt of a pension, and whose late husband was in the service of the Crown.

The allowances may not reduce the tax payable below an amount proportionate to the tax which would be payable if the whole income (British and foreign) were subject to tax.

A person living abroad for the sake of his health has an investment income of £1,050 (British £700 and Foreign £350). His allowances are, self £135 and wife £90. The tax payable on this net amount of £825 is £213 15s., but he may not pay less than £142 10s. ($£213\ 15s. \times \frac{2}{3}$) though tax on £700 - £225 is only £108 15s.

SPECIMEN ASSESSMENTS AND CLAIMS FOR REPAYMENT.—**Exemptions.** Section 18 of the Finance Act, 1920, provides that a married taxpayer may deduct from his assessable income £225, and an unmarried taxpayer, £135 (see p. 964); consequently total exemption can be claimed if the assessable income does not exceed these limits. A limited company or corporation, not being an individual, cannot claim this relief.

Example 1. Assume that an individual is called upon to make a return of income chargeable under Schedule D, that his total income for the past three years has been £312 per annum, and

that he does not pay any ground rent, annuities, interest or other charges thereout. He is a married man with two children under 16 years of age. Having filled up that part of the form relating to untaxed income (page 2) he then proceeds to enter the same amount on the "claim for allowance or deduction" (page 3) showing the total amount of his income from all sources, less charges, this being £312. On page 4 he will also fill up Sections F and J referring to the allowances for wife and children respectively. Having completed and signed the form, he will forward it to the Inspector of Taxes, when the Inspector, having satisfied himself that the claim is correct, certifies that claimant appears to be entitled to exemption. The following will show that this is the case—

Total income	£312
Deduct one-tenth earned income	31

Assessable income	£281
Deduct marriage allowance	£225
" children's "	63

288

nothing to assess.

Example 2. The income of a retail business of an individual on an average of the past three years has been £200, out of which he pays interest on loan, amounting to £5. He has, in addition, dividends from investments bringing in £15 per annum, this amount being the gross amount from which tax is deducted before receipt. He enters his income of £200 on the statement of untaxed income for assessment under Schedule D, and also fills up page 3 ("Claim for allowances or deduction"), which will appear as follows—

Income arising from business	£200
Income arising from dividends, gross	15

£215

Charges (interest on loan)	5
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Total amount of income from all sources, less charges	£210
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If this taxpayer is a married man he will fill up Section F on page 4 of the form. As he is

entitled to a deduction of one-tenth of his earned income, and £225 the allowance granted to a married man, clearly this would be a case for exemption. When completed the form would be forwarded to the Inspector, who if satisfied as to the accuracy of the figures, will certify that the claimant appears to be entitled to total exemption under Schedule D, but in doing this, relief will be extended to the income arising from the business, £200. The claimant has already paid by deduction Income Tax on the dividends received by him, and in order to obtain the benefit of the balance of the exemption to which he is entitled, by getting a repayment of tax deducted from these dividends, he has to claim repayment, which is dealt with by the local Inspector of Taxes. A form for the purpose may be obtained from the Inspector, on which the claimant is required to set out full particulars of his income and the amount he claims, at the same time making a declaration that the account is a true one, and that he was resident in the United Kingdom for the period covered by his claim. It is also necessary to furnish evidence as to the deduction of tax from the dividends received. This takes the form of the counterpart of the dividend warrant in the case of dividends, or, if none is issued, a certificate signed by an officer of the company showing the amount of tax deducted. A similar certificate signed by the party deducting tax is required in respect of interest received, but for dividends from stocks inscribed at the Bank of England, Government annuities, and payments through the Supreme Court Pay Office, certificates are not required. Full information regarding these has to be furnished, however, in order that the deduction of tax may be traced by the Claims Department.

In the illustration being considered, the claimant will attach the counterpart of the dividend warrant to his repayment claim, the particulars of income and charges appearing therein as follows—

The claim would be in the amount of £3 (*i.e.* the net amount of the Income Tax borne by

	Annual Amount of Income from each source.	Amount of Income Tax paid on or deducted from each source of Income.
Income arising from business	£ 200 0 0	£ 0 0 0
Dividends on Investments (giving particulars)	15 0 0	4 10 0
	215 0 0	4 10 0
Less Charges on Income— Interest on Loan	5 0 0	1 10 0
Total Amount of Income, less charges and amount of Income Tax thereon	£210 0 0	£3 0 0

the claimant). In due course a money order for this sum would be received from the Secretary of Inland Revenue.

The taxpayer has suffered tax to the extent of £4 10s., but as he recoups himself to the extent of £1 10s. by way of deduction of tax from the interest which he pays he is entitled to the return of £3 only.

A claim for repayment of tax will not be admitted unless made within three years of the close of the year to which it relates.

It may be here mentioned that, although a dividend has been received from a company "free of tax," a claim for return of tax thereon may still be forwarded, tax having been paid by the company on the profits distributed as dividend. The amount that has to be entered in the inner column of the claim as being the dividend received, has to be such sum as, when tax is deducted from it at the rate in force for the year in respect of which the claim is being made, will give the amount of dividend received. Thus, in a year with income tax at 6s. in the £, a dividend of £14 is received "free of tax." The amount to be claimed is £6 (viz., 6s. in the £ on £20) not 6s. in the £ on £14. The reason of this is that, whether a dividend is declared "free of tax" or "less tax," the paying company has already paid or will pay the tax on the profits so distributed. Declaring "free of tax" merely means that a calculation of tax has been made *before* arriving at the declared rate; whereas in the case of declaring "less tax," the declared rate is subject to a deduction of tax. Thus, when income tax is at 6s. in the £ a dividend of 14 per cent. "free of tax" is the same as a 20 per cent. dividend "less tax."

INCOMES OF CHARITIES, ETC. The incomes of charities are exempted by Section 61 of the 1842 Act, if arising from sources otherwise assessable under Schedule A, by Section 88 of the same Act under Schedule C, and Section 105 under Schedule D. Charities have been defined as being trusts "for the relief of poverty, for the advancement of education, for the advancement of religion, and for other purposes beneficial to the community." (See *Special Commissioners v. Pemsel*, 3 Tax Cases 53.)

Where tax has been deducted from income before receipt, a claim for repayment of the tax so deducted is made to the Special Commissioners.

EXAMPLE 3. Mr. X has an income from his business of £400, which amount has been agreed with the Inspector of Taxes as being his statutory income therefrom, he has investments bringing in £50 (before deduction of tax), his wife is in receipt of taxed income of £150 (before deduction of tax), and he pays £30 as annual interest on loan.

In order to obtain the benefit of any allowance that he may be entitled to, he should take similar

steps to those of the individual above referred to who has claimed total exemption by reason of his income from all sources being below the taxable limit. He fills up his return of untaxed income and the claim for allowances, as already explained.

The position would be as shown below—

Total income	£570
Deduct one-tenth earned income	40
Assessable income	£530
Deduct personal allowance	225
	<u>£305</u>
Chargeable £225 at 3s.	33 15 0
80 at 6s.	24 0 0
	<u>£57 15 0</u>
Add tax deducted by the taxpayer on the annual interest paid £30 at 6s.	9 0 0
	<u>£66 15 0</u>
Deduct tax on income already taxed—£200 at 6s.	60 0 0
leaving a liability of	<u>£6 15 0</u>

Example 4. Mr. A, an unmarried man carrying on a business, has agreed his profits with the Inspector of Taxes as being £130, his other income consists of £230 taxed dividends, the amount shown being before deducting tax. He has no charges on his income.

His Income Tax return and claim for allowance would show his total income as being £360, made up as follows—

Profits from business—untaxed	£130 0 0
Income from dividends—taxed	230 0 0
Total income from all sources, less charges	<u>£360 0 0</u>
His liability total would therefore be less one-tenth of £130	£360 13
deduct personal allowance, say	<u>£347 135</u>
Taxable income	<u>£212</u>
Chargeable at 3s.	£31 16 0

As this taxpayer has suffered tax by deduction of £230 at 6s., £69 0s. 0d., he will make a claim for repayment of £37 4s. 0d., representing the difference between the sum for which he is liable, and the amount which has been deducted from his dividends.

Example 5. A taxpayer is in receipt of directors' fees amounting to £360 during the Income Tax year 1921-22, has not any other income or charges thereon. He has two children under 16 years of age living at the commencement of the year of assessment.

His return would be made under Schedule E, on which he would return as untaxed income directors' fees amounting to £360.

In the spaces reserved for the purpose of a claim for wife and children he would set out particulars.

An assessment under Schedule E would be arrived at as follows—

Directors' Fees	£360
less one-tenth	36
	<hr/> £324
Marriage allowance	£225
Children's allowance	63
	<hr/> 288
	<hr/> £36
£36 at 3s.	£5 8 0

Claim of a Spinster Marrying during Year of Assessment. The income of a spinster for the year in which she marries is that accruing to her from the commencement of the year of assessment to the date of her marriage, as after that her income becomes part of the statutory income of her husband. It would not appear, even under Section 31 of the Income Tax Act, 1918, that her income from the date of her marriage to the end of the year of assessment could be separately assessed from her husband's, as application for separate assessment is required to be made within six months before the 6th day of May in any Income Tax year.

Such a woman would be entitled to any allowance, abatement, exemption, etc., determined by the amount of income which was receivable up to the time of her marriage.

A woman marries on 6th Oct. Her earned income to that date is £130 which is reduced to £117 by the 10 per cent. allowance. She is not liable to tax though her income is at the rate of £260 per annum.

Partnerships. Treatment of Partners' Rights to Abatement and Relief.

For examples as to Income Tax see page 970.

For examples as to Super-tax see page 975.

The Income Tax Act, 1918, Section 20 enacts—

The following persons having joint interests, that is to say—

(a) Coparceners, joint tenants, or tenants in common of the profits of any property; and

(b) Joint tenants, or tenants of land or tenements in partnership, being in the actual and joint occupation thereof in partnership, who are entitled to the profits thereof in shares; and

(c) Partners carrying on a trade, profession or vocation together who are entitled to the profits thereof in shares, may claim exemption, abatement or relief under the preceding provisions of this Part of this Act according to their respective shares and interests, and any

such claims which are proved to the satisfaction of the commissioners to whom they are made, may be dealt with in the same manner as in the case of several interests.

Provided as follows—

(1) Profits arising from the occupation of lands shall not be separately charged if the lands are let or underlet without the lessor relinquishing the possession thereof, or if the lessee is not exclusively in the possession and occupation of the lands;

(2) The income of a partner from a partnership carrying on any trade, profession or vocation shall be deemed to be the share to which he is entitled during the year to which the claim relates, in the partnership profits, such profits being estimated according to the several rules and directions of this Act.

It will be seen from this section that the income from a partnership is the share of the statutory profits of the partnership to which the partner is entitled in the year of assessment.

The share to which a partner is entitled may include salary, or interest on capital, or both, which must be taken into account, when arriving at the amount of the share, at the amount receivable during the year of assessment. Controversy has been busy on the point as to whether the share referred to in the section quoted above should include the whole of a partner's interest in the partnership, whether from interest on his capital, from his salary, or from his portion of the balance of profits remaining after charging partner's interest on capital, and salaries. It does not, however, appear to be an unreasonable construction to put upon the term to claim that it does, and the Income Tax authorities act on that assumption.

Another point arises where a partner lends money to a partnership over and above his capital, and receives interest on the loan so made. Inspectors urge that the interest so received is "unearned" income, although the partner may be instrumental in earning the profits out of which such interest is paid.

Double Assessment. Claim under Section 151 of the Income Tax Act, 1918. This section provides that, where a person has been twice assessed by error in respect of the same source of profit for the same year, on applying to and satisfying the Commissioners for General Purposes he can obtain a withdrawal of the double assessment, and repayment of such amount as he may have overpaid. Claim under this section must be made within three years of the end of the year of assessment.

In the cases of *London County Council v. Attorney General* (1901) 4 Tax Cases 265, and *Attorney General v. London County Council* (1907) 5 Tax Cases 242, the London County Council

sought to retain out of tax deducted on payment of loan interest, such sums as represented tax deducted from receipts from rents during the same year, and tax paid under Schedule A upon lands occupied by the Council. The Crown objected and claimed for the tax deducted from loan interest. It was held that the Council could retain tax on interest paid out of taxed sources, but was not so entitled as regards the tax paid on property occupied by itself.

[NOTE. Under Arrangement B that the Board of Inland Revenue have with building societies, a borrower whose total income from all sources does not exceed the exemption limit is not to be charged for the mortgage interest that he pays in full to the building society; if he is charged, the Board will allow repayment under a claim for double assessment.]

Setting off Loss of one Concern against the Profit of Another. Under the Income Tax Act, 1918, Schedule D, Cases 1 and 11, Rule 13, a person may set off the loss of one business against the profits of another, so long as they are both assessable under Schedule D. The practice in such a case is to arrive at the statutory loss or profit of the respective businesses independently and deduct the one from the other, thus—

BUSINESS A.

Adjusted Profit for year ended 31st March, 1919	£	700
Adjusted Profit for year ended 31st March, 1920		650
Adjusted Profit for year ended 31st March, 1921		750
		<hr/>
Profits for three years	£2,100	
	<hr/>	
Average profit for 1921-22	£700	

BUSINESS B.

Adjusted Loss for year ended 31st Dec., 1918	£	310
Adjusted Loss for year ended 31st Dec., 1919		360
		<hr/>
Less Adjusted Profit for year ended 31st Dec., 1920		70
		<hr/>
Net Loss for three years	£600	
	<hr/>	
Average Loss for 1921-22	200	
	<hr/>	
Assessment for 1921-22 would be	£500	

The deduction of a loss under this section should be made when returning income assessable under Schedule D.

Claim in respect of Losses under Section 34 of the Income Tax Act, 1918. Under Sub-Section 1 of this section—

(1) "Where any person sustains a loss in any trade, profession, employment or vocation, carried on by him either solely or in partnership, or in the occupation of lands for the purpose of husbandry only, or in the occupation of woodlands in respect of which he has elected to be charged to tax under Schedule D, he may upon giving notice in writing to the inspector within six months after the year of assessment, apply to the General Commissioners or to the Special Commissioners, for an adjustment of his liability by reference to the loss and to the aggregate amount of his income for that year estimated according to this Act.

(2) "The Commissioners shall, on proof to their satisfaction of the amount of the loss, and of the payment of tax upon the aggregate amount of income, give a certificate authorising repayment of so much of the sum paid for tax as would represent the tax upon income equal to the amount of loss, and the certificate may extend to give any exemption, abatement, or relief depending upon total income from all sources, authorised by this Act.

"Upon the receipt of the certificate the Commissioners of Inland Revenue shall cause repayment to be made in conformity therewith.

(3) "If any person shall be guilty of any fraud or contrivance in making any application under this Section, or in obtaining any such adjustment or certificate as aforesaid, he shall forfeit the sum of fifty pounds.

(4) "Where repayment has been made to a person for any year under this Section, he shall not be entitled, in computing the amount of the assessment for any subsequent year, to a deduction of any portion of the amount in respect of which such repayment has been obtained."

It will be observed that the benefit of this section differs from that referred to in Income Tax Act, 1918, all schedules, Cases 1 and 11, Rule 13, which allows the setting off of a loss on one concern against the profits of another assessable under the same Schedule D, inasmuch as it allows a set-off of loss from the occupations referred to, against taxed income, no matter under what schedule assessment has been made.

The loss mentioned is the actual statutory loss of the year of assessment, which it has been shown above does not necessarily, or usually, correspond with the loss shown by the accounts of a business. It should be noted that the loss is a general loss, not a particular loss, whereby the profits have been diminished.

The repayment, it will be seen under Sub-Section 2, is upon the loss to the extent that income can be shown to have been taxed in the year of assessment. The extension of the benefit to exemption or relief by way of abatement may prove useful, but otherwise the benefit is largely

equivalent to the rate of Income Tax on £50 is derived by putting forward the claim. Thus—

	Claim made.	Claim not made.
1918-19 Assessment, allowing for repayment	£ 100	£ 400
1919-20 " " " "	200	100
1920-21 " " " "	140	40
1921-22 " " " "	50	—
Total Assessments	£490	£540

Briefly, it may be stated in relation to the operation of this section, that it is advantageous to claim (a) when the loss is likely to continue or only small profits are anticipated; (b) when the business is to be discontinued; (c) when the rate of Income Tax is not likely to increase; (d) when a loss arises in the first or second year of setting up a business; and (e) when the benefit of extra abatement, relief, or reduction of Super-tax obtained for the year in respect of which the claim is made is not counterbalanced or exceeded by possible loss of abatement, relief, or reduction of Super-tax which might arise by not being able to bring the loss into average in any subsequent year.

Claim in respect of a Profession, Trade, or Vocation set up within Three Years. The Income Tax Act, 1918, Schedule D, Cases 1 and 11, Rule 8 (1), provides:

"Where a person charged or chargeable with Tax in respect of any trade, profession, or vocation which has been set up or commenced within the period of three years upon the average of which the profits or gains are to be taken, or within the year of assessment, proves at the end of the year of assessment to the satisfaction of the Commissioners by whom the assessment has been or can be made that the actual profits or gains arising from the trade, profession, or vocation in the year of assessment fall short of the profits or gains as computed in accordance with this Act, he shall be entitled to be charged on the actual amount of the profits or gains so arising, instead of on the amount of the profits or gains so computed, and, if he has paid the full amount of the tax on the profits or gains so computed, he shall be entitled to repayment of the amount overpaid."

From this it will be seen that, if the profits of the year of assessment, as adjusted for Income Tax of a new business set up within three years, fall short of those upon which assessment has been made, the taxpayer is entitled to have the assessment reduced to the profits of the year of assessment, or if he has already paid Income Tax thereon to claim repayment of the tax so overpaid. The claim has to be proved at the end of

the year of assessment, and the business must be set up within the period mentioned. Starting in business by purchasing an established business does not constitute setting up a business, nor does a company set up a business where it has been converted from a private firm. In other words, a succession to a business does not involve setting up a new business.

The following example shows the operation of the section—

Example. A business was set up on the 6th April, 1915, and the owner, a limited company, was assessed on estimated profits amounting to £750. Its actual profits, as adjusted for Income Tax purposes for that and the three succeeding years, were £500, £400, £330, and £360 respectively. The statement hereunder explains the company's rights in the matter—

	Income as assessed.	Actual Income.	Excess upon which tax is recoverable or assessment reducible.
Year ended 5th April, 1916, as estimated	£ 750	£ 500	£ 250
Year ended 5th April, 1917, based on income of previous year	500	400	100
Year ended 5th April, 1918, based on average of actual income of two previous years, viz.— Year to 5/4/1916 . . . £500 " " 5/4/1917 . . . 400	Two years . . . £900	£150	£330
Year ended 5th April, 1919, based on average of actual income of three previous years, viz.— Year to 5/4/1916 . . . £500 5/4/1917 . . . 400 5/4/1918 . . . 330	£1,230	410	360

Claim in respect of Discontinuance of Profession, Trade, or Vocation. The Income Tax Act, 1918, Schedule D, Cases 1 and 11, Rule 8 (2), reads—

"Where a trade, profession, or vocation is discontinued in any year, any person charged or chargeable with Tax in respect thereof, shall be entitled to be charged on the actual amount of the profits or gains arising therefrom in that year, and shall also, if he proves to the satisfaction of the Commissioners, by whom the assessment has been or could have been made, that the total amount of the Tax paid for the three previous years in respect of that trade, profession, or vocation, exceeds the total amount which would have been paid if he had been assessed for each of those years on the actual amount of the profits or gains arising in each year, be entitled to repayment of the excess."

The section, therefore, gives the right to the owner on the discontinuance of a business—

1. To be charged on the actual results of the year in which the discontinuance took place.

2. To be repaid the amount by which the tax paid by him during the three previous years exceeds the amount of tax, if calculated on the actual "Income Tax" results of those three years. *i.e.* If one of the three years showed a loss, this loss could not be deducted from the profits of the two remaining years.

It should be noted that, although the taxpayer discontinues his business, when he sells or otherwise disposes of it, as the business itself is not discontinued, he is not able to claim under this section.

The two examples given below show (a) where it is advantageous to claim repayment for all four years, and (b) where a claim should be only made in respect of the first three years and not in respect of the final year.

Two businesses were "discontinued" on 5th April, 1918, their respective profits for the six years having been—

Year ended 5th April, 1913 .	Business Business	
	(a).	(b).
" " " 1914 .	£1,200	£1,200
" " " 1915 .	1,000	1,050
" " " 1916 .	1,100	600
" " " 1917 .	600	450
" " " 1918 .	400	150
" " " 1919 .	200	150
" " " 1920 .	100	300

The following assessments have been made in the case (a) upon which tax had been duly paid—

	Assessment.	Actual Income.	Amount upon which tax is recoverable.
For Income Tax year 1915-16 .	£1,100	£600	£500
" " " 1916-17 .	900	400	500
" " " 1917-18 .	700	200	500
" " " 1918-19 .	400	100	300
Total . . .	£3,100	£1,300	£1,800

The tax would be repayable at the rates of the different years.

In the case of business (b), the assessments were—

	Assessment.	Actual Income.	Amounts upon which tax is recoverable.
For Income Tax year 1915-16 .	£950	£450	£500
" " " 1916-17 .	700	150	550
" " " 1917-18 .	400	150	250
" " " 1918-19 .	250	300	—
Total . . .	£2,300	£1,050	£1,300

For the final year it would be more advantageous to pay on the assessment instead of the actual profit.

Rights on Succession. The Income Tax Act, 1918, Schedule D, Miscellaneous Rules, 3, reads as follows:

(1) "If a person charged under this Schedule, whether the computation has been made on the profits of one year or on an average of years, ceases to carry on the trade, profession, employment or vocation in respect of which the assessment was made, or dies or becomes bankrupt, before the end of the year of assessment, or from any other specific cause is deprived of or loses the profits or gains so computed, he or his executors or administrators may, within three months after the end of the year of assessment, apply to the General Commissioners of the division for the amendment of the assessment.

(2) "The General Commissioners, on proof of their satisfaction that Paragraph (1) of this Rule applies to the case, shall cause the assessment to be amended or vacated, and give such relief as is just, and shall, if necessary, direct repayment to be made of any sum which has been overpaid.

(3) "A person who has succeeded to the trade, profession or vocation of a person charged shall, subject to the provisions of Rule 9 of the rules applicable to Cases 1 and 11, be liable to pay the full tax charged without any new assessment, and no relief under this rule shall be granted in any such case unless the person so succeeding proves, to the satisfaction of the commissioners, that the profits or gains have fallen short, from some specific cause, since, or by reason of, the succession.

By Rule 11 applicable to Cases 1 and 11 of Schedule D, it is provided—

"If within the year of assessment or the period of average upon which the assessment is to be based a change occurs in a partnership of persons engaged in any trade or profession, by reason of death, or of dissolution of the partnership as to all or any of the partners, or by the admission of a new partner, or if any person succeeds to a trade or profession, the tax payable in respect of the partnership, or any of the partners, or of the person so succeeding shall be computed according to the profits or gains of the trade or profession during the respective periods prescribed by this Act, notwithstanding the change or succession, unless the partners or the person succeeding to the trade or profession prove to the satisfaction of the Commissioners that the profits or gains have fallen or will fall short from some specific cause, to be alleged to them, since such change or succession took place, or by reason thereof."

It will be seen that, although the words of

the above rules are somewhat similar, one refers to cases where a change of proprietorship of a business takes place before the time of making the assessment, and gives the directions to be followed, that is, the assessment is to be based on an average of years as though no change had taken place. But in the case of a change in a partnership being caused by dissolution, or the death of a partner, or, in the case of a business changing hands, the partners, or such persons succeeding to the business, have the right of appearing before the Commissioners to prove that some *specific cause* has caused, or will cause, the profits of the business to fall short since the change took place, and that application of the average system of assessment would, therefore, be inequitable. Failing proof to this effect the assessment will be based on the average of previous years as though no change in proprietorship has occurred.

Section (134) deals, *inter alia*, with cases of succession, where assessment has been made, and a *specific cause* of fall in profits proved within three months of the end of the year of assessment. Either amendment of the assessment will then be made or else repayment made of the tax overpaid, but here again the specific cause must be proved to have arisen since the change. The section also refers to cases where a person charged to Income Tax dies, or becomes bankrupt or insolvent, and it would therefore appear that the personal representatives of the deceased, or the trustee of a bankrupt, should claim under this section. If, however, a discontinuance of the business takes place in consequence of the death or bankruptcy, the Income Tax Act, 1918, Schedule D, Cases 1 and 11, Rule 8 (2), would apply, and the taxpayer, either himself, or by his representatives, could claim adjustment, not only of his profits of the year of assessment, but also of the previous three years. If a person be deprived or lose the profits or gains on which duty has been charged, he should apply to the Commissioners within the stipulated time, and claim adjustment under this section.

The rule as to succession applies (a) in the case of a business being converted into a company (see *Ryhope Coal Co., Ltd. v. Foyer* (1881) 1 Tax Cases 343), when it was decided that such a conversion did not constitute a business being set up and commenced, but was a succession under the rule; (b) on the purchasing of an existing business (see *Bell v. National Provincial Bank of England* (1904) 5 Tax Cases 1), when it was held that on a banking business and premises being purchased at Wolverhampton, and business being carried on there by the purchasing company, although the profits and outgoings were merged in the purchasing company's profits and outgoings, succession under the rule took place; and (c) on

a new partner entering a partnership, or an old one going out, the succession in the latter instance being that of the remaining parties to the whole business.

"SPECIFIC CAUSE." The following are instances where succession takes place owing to loss by "specific cause."

1. Assume a partner in a profession carried on by two or more persons goes out of the partnership or dies, thus causing a decrease in the profits, owing to the fact that part of the connection, which depended on his personality, followed him, or was lost. That there had been "specific cause" would be upheld in such an instance.

2. Also if a partner on retiring, or dying, withdraws his capital, thus involving his successors in borrowing from a bank and paying interest thereon. In so far as the interest is not "annual" interest, a claim that a "specific cause" had arisen would be supported. The same remark applies if a paid servant were employed in the place of a retiring working partner.

3. In *Ryhope Coal Co. v. Foyer* (1881) 1 Tax Cases 343, it was held that an extraordinary depression in the iron and coal trades, which adversely affected profits, was a "specific cause."

4. A private firm is converted into a limited company. The payment of directors' fees would be a "specific cause" to explain the falling off in the amount of subsequent profits. The figures as adjusted for Income Tax of the years prior to incorporation would not include partners' salaries, and a charge on the company based on those figures would be inequitable, particularly having regard to the directors' fees being assessable under Schedule E. If adjustment of assessment were not allowed in respect of directors' fees paid, the same source of income, to the extent of the fees, would be twice taxed, firstly under Schedule D, as no allowance for directors' fees or partners' salaries would have been made in arriving at the figures of the three preceding years, and secondly, under Schedule E, upon the individual directors. In such cases it is the practice for the purpose of averaging the profits of a company, to treat them as new businesses, and assess on the actual profits of the first three years.

Adjustment of Assessment under Schedule D, Cases 1 and 11, Rule 9 (1). Where a person, assessed under Schedule D, ceases, within the year of assessment, to carry on the concern in respect of which an assessment has been made upon him, and is succeeded by another person, the assessed person is entitled to an adjustment of the assessment, having regard to the period during which he carried on the business in the year of assessment. The amount of which he is relieved is chargeable upon his successor.

In such cases it is usual to apportion the charge according to the number of days during which each carried on the concern in the year of assessment.

Claim for Return of Tax on Interest not being Annual Interest paid to Banks. The Board of Inland Revenue, will, in certain cases, allow a claim for return of tax upon bank interest paid. In the case of a business assessed under Schedule D, it has been seen that it is the practice to allow the charge as a deduction in arriving at the profits. Unless some concession were made, persons paying interest to banks out of taxed income, would be doubly assessed, first by deduction of tax from the income received, and secondly by not being able to deduct tax on payment.

The procedure necessary to getting repayment is to obtain a certificate, in the prescribed form, from the bankers, giving particulars of the interest paid, stating that tax has not been deducted therefrom, and that the amount so received by the bank has been or will be included by the bank as part of their profits for assessment under Schedule D. The claimant then fills up a form, usually attached to the bankers' certificate, stating amongst other things the purpose of the loan, and setting out particulars of taxed income equal to the amount of interest upon which repayment is claimed. Vouchers should be attached verifying the amount of Income Tax paid, and the whole forwarded to the Secretary of Inland Revenue for his attention.

It has been implied that the concession is not always made. Repayment has been refused in the case of an investment company, whose assets consist of investments and loans, and whose receipts were all taxed at source. It had the power to realise any of its investments, although, under its Articles, any profit on sale could not be treated as a distributable profit.

In the case, however, of a company whose capital was invested in property, some of which was mortgaged, and who subsequently disposed of certain properties under pressure from the mortgagees, the Board allowed repayment of tax on the amount of bank interest paid.

Repayment will not be made to a trader who has borrowed from his bankers for the purpose of his business, even if there is no profit from which to deduct bank interest.

Claim for Repayment under Income Tax Act, 1918, Schedule A, V, (8). Where a taxpayer finds that, on the average of the five preceding years, the cost of maintenance, repairs, insurance and management of land (inclusive of farmhouses and buildings), or houses, etc., has exceeded the allowance of one-eighth of the gross annual value of the land and one-sixth of houses) and in the case of houses the Schedule A value does not exceed £105 in London, £90 in Scotland, and £78 elsewhere, he may claim the excess that such average shows.

The necessary procedure to be followed is, within three years of the end of the year of

assessment to furnish the Inspector of Taxes in the district in which the land or property is situated, with a statement in the form of a declaration showing the cost of the expenditure on the property, based on a five years' average ending the 31st March in the year preceding the year of assessment, or ending such other date as the Inspector may approve. On his being satisfied as to the accuracy of the declaration, he certifies that the claimant is entitled to repayment of tax upon the amount by which the average exceeds the allowance made in arriving at the net assessment.

Thus, an owner of land, the gross annual value and net annual value of which is £32 and £28 respectively, finds his average expenditure upon the property for the past five years amounts to £17. He could successfully claim for a return of tax on £13, made up as follows—

Cost of maintenance, repairs, insurance, and management on average of five years . . .	£17
Allowance, one-eighth of £32 . . .	4
Amount upon which tax is repayable . . .	<u>£13</u>

Claim under Income Tax Act, 1918, Schedule A, VII (4). Where property is unlet during the whole year of assessment, the assessment may be discharged, and if it becomes unlet *during* the year a proportionate amount of the assessment is allowed, corresponding to the period during which the property was unlet.

Claim under Income Tax Act, 1918, Schedule D, 6. As has been seen above, a farmer, under this section, where his lands are used for the purpose of husbandry only, can claim adjustment of the assessment made upon him under Schedule B by having the amount reduced to the actual amount of his profits, or, if he has paid the whole of the tax, can obtain repayment of the amount overpaid.

At the end of the year, in order to obtain the benefit of the section, he is required to furnish accounts for the year showing the results of his trading. Failing this, he must render a statement of receipts and payments on account of the farm, grouped under headings shown on the form of claim, together with the amount of live and dead stock at the beginning and end of the year in respect of which the claim is being made. If the actual value of stock is not available, a declaration as to it is required, and an estimate of any increase or decrease in value given. To the receipts have to be added the value of farm produce used by the farmer's household.

The "Income Tax" profits for the year are then arrived at by adding to the total receipts (including produce used by the household), the amount of stock at the end of the year, and deducting therefrom the (a) total payments

(including Schedule A assessment, if the owner is the occupier), and (b) the amount of stock at the commencement of the year.

APPEALS.—Under Schedules A and B. As soon as assessments under these schedules have been made, notices thereof are given either by a copy being furnished to the assessor for inspection by the parties charged, together with a public notice of date of appeal, or by advising each party charged as to the amount of his assessment, and the date of appeal. A party aggrieved by an assessment made upon him may appeal to the Commissioners in regard thereto.

If, upon appeal in respect of lands, etc., outside the Metropolis, a dispute arises as to the annual value of any lands, tenements, etc., and the Commissioners consider it necessary, or if the appellant require it, the Commissioners may direct the appellant to have a valuation of the property made by an independent expert valuer named by them. On receiving the valuer's report as to value of the property, the Commissioners are required to assess accordingly. The costs of the valuation will be paid by the appellant, if the valuation exceeds the appellant's valuation, unless the Commissioners are of opinion that such costs have not been incurred through his default, when the Collector of the district will be directed to pay.

As a rule, it will be necessary to get an appeal decided on the poor rate assessment, and this having been done, amendment of the Schedule A assessment usually follows.

Claims for adjustment of an assessment by reason of the property becoming vacant have been dealt with above.

Under Schedules D and E. A notice of assessment relating to a charge under either of these schedules is usually served in the latter part of the year, and if the recipient is not satisfied in regard to it, he may appeal against it, when he gives notice to the Inspector of Taxes to that effect. Notice of appeal must now be given within 21 days of the date appearing on the notice of charge, but prior to the 1914-15 assessments only ten days' notice was allowed. The Commissioners have power to accept notice after the period of 21 days has expired, if the person charged is prevented by absence, sickness, or other reasonable cause from making his appeal.

The appeal may be made either to the General Commissioners or to the Special Commissioners. The effect of appeal to the former is that all questions of fact are finally determined by their decision, if there is evidence before them on which to decide such questions, and the right of carrying the appeal to the High Court is restricted to questions of law. An appeal to the Special Commissioners, if either the appellant or the Inspector is dissatisfied with the decision, also enables the case to be carried to the High Court

on questions of law, or to the Commissioners of Inland Revenue on a question of fact.

It has been stated above that accounts, or schedules practically corresponding with accounts, may be called for by the Commissioners, and on notice of appeal these are demanded. In practice the result of forwarding accounts with the notice of appeal, or of attending on the Inspector with them, is that attendance before the Commissioners is very often dispensed with, if the Inspector is able to see from the figures produced that the appeal is justified. In such circumstances, the notice of assessment is amended. If, however, agreement cannot be come to with him, it will be necessary to attend at the appeal meeting. The appellant may appear in person, or, if the appeal is before the Special Commissioners, he may be represented by a barrister, solicitor, or accountant. Section 137 (3) of the Income Tax Act, 1918, requires that the accountant must have been admitted a member of an incorporated society of accountants. The General Commissioners may refuse to hear advocates in appeals before them, in which event, the appellant may proceed with his appeal before the Special Commissioners.

CASES STATED. If either the Inspector, or the appellant, be dissatisfied with the determination of the Commissioners, as being erroneous in point of law, immediately on such determination he shall declare his dissatisfaction to the Commissioners, who heard the appeal, and require a case to be stated for the opinion of the High Court thereon. Having paid a fee of 20s. to the Clerk to the Commissioners, the party requiring the case to be stated must demand the case within 21 days, and having obtained it, forward it to the High Court. A copy must also be furnished to the other party. The decision of the High Court can be contested in the Appeal Court, and, finally, in the House of Lords.

Numerous cases have been tried upon the right to revision by the High Court of the Commissioners' decision upon a question of fact, and upon this point the Lord Chancellor, in giving judgment in the case of *De Beers Consolidated Mines, Ltd. v. Howe* (1906) 5 Tax Cases 198, said: "The Commissioners, after sifting the evidence, arrived at the two following conclusions, viz., . . . *These conclusions of fact cannot be impugned*, and it follows that this company was resident within the United Kingdom for the purpose of Income Tax, and must be assessed on that footing." From this and other cases, it will be found that the High Court has no jurisdiction over questions of fact, if there is evidence before the Commissioners on which to decide such questions.

In appeals before the Commissioners, evidence of the party charged, or of any other person, may be required to be given on oath, and any accounts called for by them, they may demand shall be

supported by affidavit. They have power to increase an assessment on appeal, if it is found that the appellant has been under-assessed.

Since the case of *Rex v. The Brixton Income Tax Commissioners and Another* (1913) 6 Tax Cases 195, the Inspector of Taxes is not allowed to remain with the Commissioners when they are arriving at their decision. Until then it was the usual practice for the appellant to be asked to withdraw whilst the determination was being come to by the Commissioners. As the Inspector of Taxes remained with them, it is easy of understanding that arguments under those circumstances might be put forward, or continued, without opportunity of reply being given to the appellant. The Attorney-General, in the case referred to, stated that, although the old practice had existed for a long time, he was perfectly satisfied that the Inspector of Taxes had no right to be present when the Commissioners are considering their decision, than any other party to the appeal.

MISCELLANEOUS.—Back Duty. The Act provides in this connection that the times during which an assessment may be amended or an additional first assessment made, or during which an assessment may be made on the estate of a deceased person, shall be any time during the year of assessment, or within three years after the expiration thereof. Proceedings for the recovery of penalties may be commenced within three years next after the penalty is incurred.

It will be seen from this that no legal authority exists for recovery of back duty beyond a period of three years from the end of the year of assessment, thus profits of the tax year 1910–11, that may have escaped taxation, cannot be charged after 5th April, 1914.

If an under-assessment has been brought about by the taxpayer's failure to make a return, or by his having made an inaccurate return, he will usually find that he is pressed to pay back duties for even six or nine years. In deciding whether he shall do so, or not, he has to remember that a penalty amounting to treble duty, and a payment of £20, if the proceedings are before the Commissioners, may be imposed. With this being applied as a lever, he will usually decide to agree to pay the equivalent of duty on the profits of the additional years, prior to the period covered by the section above referred to.

Building Societies. Special arrangements, styled A and B, are made between the Board of Inland Revenue and building societies as to their assessment under Schedule D.

If assessment is made under Arrangement A—

(a) All interest is exempted if the borrower has a total income from all sources not in excess of £135.

(b) Interest, where the borrowers are not

exempt, to be charged, and the borrowers to be allowed to deduct tax from the interest payable.

(c) Property of the Society as mortgagees to be exempt, except to the extent that ground-rent may be paid.

(d) If amount of interest received, where tax has been deducted, is in excess of amount of interest paid, where tax has been deducted, the Society is repaid tax on the difference—but if the reverse is the case, an assessment under Schedule D is to be made on the amount of the difference.

If assessment is under Arrangement B—

(a) One half of the total amount received during the year prior to the year of assessment in respect of dividends, bonus, and interest on deposits is assessed on the Society under Schedule D, the remaining half being allowed as a set-off for exemptions.

(b) Property of the society as mortgagees to be exempt, except to the extent that ground-rent may be paid.

(c) Borrowers with incomes of £135 and under are not to be charged upon the amount of interest paid by them.

(d) Borrowers with incomes in excess of £135 to be repaid by the Inland Revenue tax on mortgage interest.

(e) Depositors and others not to be charged on dividends or interest received by them.

Mutual Concerns. Clubs are not usually assessable, but they are liable to pay tax on any bank interest received by them, and on any profits made from non-members. A golf club has been held liable in respect of its receipts from visitors, but the decision did not cover the method by which the profits arising from such receipts were to be calculated. (See *Carlisle and Silloth Golf Club v. Smith* (1913) 6 Tax Cases 198.)

Gate moneys received from the public would be assessed in respect of profits arising therefrom. Mutual insurance companies are not assessable on the profits arising from the premiums of participating policy-holders.

Interest. It has been seen above that if annual interest is paid, tax is deducted by the payer, who has to account for the sum so deducted.

Where a person pays interest out of profits for assessment under (say) Schedule D, he is not separately charged on the interest from which he has deducted tax, as under Rule 4 of the 1st Case of Schedule D he is charged indirectly on it by the non-allowance of annual interest as a charge against profits.

Where interest is not annual interest, the assessment is made under Case 3 of Schedule D, on the recipient. Bank and short loan interest as a deduction from profits, and as the subject matter of a claim for repayment, is considered on pages 957 and 962.

Annuities and Other Annual Payments. On making such payments, the payer has to deduct tax and is accountable to the Revenue as in the case of yearly interest. Deduction of tax must always be made at the highest rate in operation (see p. 947.)

Investment Companies. Where the income of such a company solely consists of dividends and interest, the whole is assessable to Income Tax, either by deduction or direct assessment, irrespective of the fact that expenses, such as office expenses and directors' fees, are paid. If, however, the company deals in securities within the scope of its objects, the profits resulting therefrom would be assessable under Schedule D, when allowable expenses could be taken into account.

Depreciation of investments are not able to be set against profits on sale of investments.

Where the income of a company is largely received from interest and dividends, and the company also carries on a trade (*e.g.* an insurance company) the Revenue Authorities have the right to assess either on the interest and dividends (if untaxed) under Case 3 of Schedule D, or on the profits under Case 1 of that Schedule. The latter method will only be adopted if the profits exceed the amount of interest and dividends received. In the case of *Revell v. The Edinburgh Life Assurance Co.* (1906) 5 Tax Cases 221, the company had received untaxed interest. It was held that such interest was assessable, although the company claimed that a loss had been made after deducting taxed income under Section 23 of the 1890 Act.

Hire Purchase Agreements. As part of payments made in respect of such agreements are in respect of hire, a deduction may be made in arriving at the assessable profits under Schedule D of a proportion of the payment. The usual method of arriving at the annual amount to be charged is to deduct the cost that would have been charged for the hired article if purchased outright from the total amount payable under the terms of the agreement, and to divide the difference by the number of years over which payments are spread.

In the case of railway wagons, an allowance for depreciation can also be obtained.

Income Tax Paid in Advance. A person may pay his Income Tax in advance of the date when it actually becomes due, in which case a discount

at the rate of $2\frac{1}{2}$ per cent. per annum is allowed on the amount payable.

Recovery of Income Tax. If a person refuses to pay the sum charged upon him, the collector may, without further authority, distrain. The distress so levied must be kept for five days at the cost of the person refusing to pay. If, during that time, payment is not made, the distrained goods, after appraisal, are sold by public auction, and the surplus (if any) over and above the Income Tax and costs is returnable to the taxpayer.

For the purpose of levying the distress, the collector may, under warrant from the Commissioners, break open premises in the day time. The distraint will be upon the taxpayer's premises, or his goods and chattels. It will be extended to a third party's goods and chattels, if upon the debtor's premises, and the claim is for duties payable under Schedule A. If insufficient goods are leviable, the defaulting taxpayer is liable to be committed to prison by the Commissioners.

Liquidators and Trustees in Bankruptcy and Income Tax. Under the Bankruptcy Act, 1914, all assessed taxes (including Income Tax) due from a bankrupt, and having become due and payable within twelve months next before the date of the receiving order up to the 5th April next before that date, and not exceeding in the whole one year's assessment, are preferential and rank equally for payment with other preferential creditors.

Under the Companies (Consolidated) Act, 1908, all assessed taxes (including Income Tax) assessed on a company up to the 5th April next before the date of the winding-up order in compulsory liquidation, or the date of winding-up resolution in the case of voluntary liquidation, and not exceeding one year's assessment, are preferential, and rank equally for payment with other preferential debts.

The Inland Revenue would rank with the ordinary creditors in either bankruptcy or liquidation for such amount as exceeds a year's assessment, or is assessed in respect of a period after the 5th April prior to the date of the receiving order or winding-up resolution, as the case may be.

Personal liability, on the grounds of misapplication of funds, attaches to a liquidator, who pays away all assets of a company without making provision for a Crown debt for Income Tax. (See *In re The Watchmakers' Alliance and Ernest Goode's Stores, Ltd.* (1905) 5 Tax Cases 117.)

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